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Article

Danish Dynamite: The 26 February 2019 CJEU Judgments in the Danish Beneficial Ownership Cases*

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On 26 February 2019 the Grand Chamber of the Court of Justice of the European Union ('CJEU') delivered two groundbreaking judgments in the field of tax abuse. These judgments are known as the Danish beneficial ownership cases and relate to withholding tax exemptions provided for by the Interest and Royalty Directive (joined cases C-115/15, C-118/16, C-119/16 and 299/16) and the Parent-Subsidiary Directive (joined cases C-116/16 and C-117/16). They contain numerous interesting statements, notably the confirmation for the first time that the direct tax Directives are controlled by the general principle of EU law according to which EU law cannot be relied upon for abusive purposes (the 'abuse of rights principle'). Furthermore, the CJEU also interprets the much debated concept of 'beneficial ownership' ('BO') for the first time. In this contribution, the authors will analyse the judgments of the CJEU as regards the abuse of rights principle and the BO concept.

1 Facts and EU law provisions at stake[1]

In the late 1990s/early 2000s Denmark was a very attractive country to establish (intermediary) holding companies as it did not levy withholding tax on dividends paid to foreign parent companies, regardless of their residence. In addition, it did not levy withholding tax on interest paid to non-resident lenders either. Following criticism from the EU Ecofin Council's Code of Conduct group, Denmark had to change its policy and in 2001 respectively 2004 it introduced withholding tax on dividends and interest, subject, however, to the exemptions provided for in the Parent-Subsidiary Directive ('*PSD*') and the Interest and Royalty Directive ('*IRD*').[2]

Near the end of 2006 the Danish Minister of Finance launched a series of investigations against a number of Danish companies that had been acquired by non-European private equity funds under highly leveraged structures. Typically, companies were interposed in an EU Member State between the Danish company distributing the dividends or paying the interest and the private equity funds, allowing the interposed companies to avail themselves of the exemption of dividend or interest withholding tax in Denmark under the provisions of the PSD or IRD. Smart selection of the Member State of establishment of the interposed company and smart structuring of the funding of that company allow the channelling of dividends or interest from Denmark to countries outside the EU with little or no tax leakage within the EU (tax free EU exit).[3] Such kind of tax optimization schemes are called Directive shopping.[4]

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1 As we are not Danish tax practitioners, for the description of Danish law we have relied on the writings of Danish authors and in particular on: S. J. Baerentzen, *Cross-Border Dividend and Interest Payments and Holding Companies – An Analysis of Advocate General Kokott's Opinions in the Danish Beneficial Ownership Cases*, ET 343–53 (2018) and H. S. Hansen, *The Great Hypocrisy – The 'Beneficial Owner' Cases*, Danish J. Taxes & Duties – TfS 537 et seq. (2011) (translation). For the detailed facts of the cases, we refer to the writings of the first-mentioned author.

2 The cases discussed in this contribution are governed by Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries in different Member States, as amended by Directive EC 2003/123/EC of 22 Dec. 2003 and by Directive 2003/49/EC of 3 June 2003 on the common system of taxation applicable to interest and royalty payments made between associated enterprises of different Member States.

3 Of course, apart from the Danish corporate tax paid on the profits of the Danish companies.

4 L. De Broe, *International Tax Planning and Prevention of Abuse, A Study under Domestic Law, Tax Treaties and EC Law in Relation to Conduit and Base Companies*, IBFD 20–23 (2008). The term paraphrases the term '*treaty shopping*'. '*Treaty shopping*' refers to the situation where a person resident of a State (R) who expects to derive dividends, interest or royalties from another State (S) sets up an entity in a 3rd State (X) that will receive such income in a way i.e. more tax beneficial than if such income were to be paid directly from State S to the State R resident. The tax advantage results from the fact that the tax treaty between S and X provides for lower withholding taxes than the rate that would have applied if the payments would have been made directly from S to R. In other words, the R resident shops into an otherwise unavailable treaty (S/X) by setting up an entity in State X that receives the income arising in S and pays it on to the State R resident. '*Directive shopping*' refers to the situation where a person who does not qualify for the benefits of the PSD or IRD (e.g. because he is established outside the EU) shops into the Directive by setting up a controlled entity in an EU Member State that receives dividends or interest from a subsidiary or associated company established in another Member State free of withholding tax in that State.

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The Danish tax authorities claimed that the interposed companies are so-called conduit companies, the only function of which is to channel income from Denmark to non-EU countries (including tax havens) and that they are not the BO of the dividends or interest. On that ground they denied those companies the exemption of Danish withholding tax. The cases have been litigated before Danish courts and in 2016 the High Court of Eastern Denmark brought six cases before the CJEU for preliminary ruling, two dealing with the PSD and four with the IRD.[5] The cases concern dividends distributions and interest payments that took place between 2005 and 2012.

For the years under dispute, Article 1 (2) of the PSD read as follows: '*This Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse*'.[6]

For the years under dispute, the relevant provisions of the IRD were the following. Article 1 (1): '*Interest […] arising in a Member State shall be exempt from any taxes imposed on those payments in that State […], provided that the beneficial owner of the interest […] is a company of another Member State […]*'; Article 1 (4): '*A company of a Member State shall be treated as the beneficial owner of the interest […] only if it receives those payments for its own benefit and not as an intermediary, such as an agent, trustee or authorized signatory, for some other person*'; Article 5 (1):'*This Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse*', and finally Article 5 (2): '*Member States may, in the case of transactions for which the principal motive or one of the principal motives is tax evasion, tax avoidance or abuse, withdraw the benefits of this Directive or refuse to apply this Directive*'. It clearly follows from the wording of provisions like Article 1 (2) of the PSD and Article 5 of the IRD that they do not compel the Member States to enact anti-abuse measures in their domestic laws implementing the PSD or IRD. The Member States have reserved their competence in this respect and exercise discretion on whether and how they will implement measures in domestic law that aim at preventing abuse of the provisions of the PSD or IRD.[7]

Denmark did not implement specific measures preventing abuse of the PSD or IRD under Article 1 (2) PSD or Article 5 IRD. It was only in 2015 that Denmark enacted a general anti-avoidance rule (GAAR) in its domestic tax law. Moreover, at the time of the payments under dispute, the concept of BO was not known in Danish tax law. The tax authorities equated the term BO to the Danish concept of '*rightful income recipient*', a judicially developed concept according to which the rightful recipient is the person to whom the income is allocated for tax purposes, regardless of formal appearances, i.e. the civil law owner of the shares or the civil law creditor of the loan. However, it seems that during the litigation the Danish tax authorities changed their position and did no longer maintain that the concepts of BO and rightful income recipient were synonyms. They rather seemed to have pressed the argument that the interposed companies were not the BO under the terms of the 2003 OECD Commentary on Article 10 and 11. Danish tax law also seems to know a judicially developed concept, called the 'reality'-principle which operates as a substance over form-principle. However, the parties involved in the litigation agreed that that principle was not capable of setting aside the arrangements in the case at hand.[8]

2 Questions referred to the CJEU

The referring Danish court brought a series of questions to the CJEU. Following the request of the Danish government the PSD and IRD-cases have been referred to the Grand Chamber of the CJEU and the CJEU allowed a joint hearing of all the cases. In its judgments the CJEU rephrases and pools several of the questions raised by the referring court and answers them simultaneously.

In the PSD-case, the CJEU first answers the question of the referring court of whether the combating of fraud or abuse, as permitted by Article 1 (2) of the PSD, requires that the Member State in question has adopted specific domestic or treaty-based anti-abuse provisions or that national law contains general provisions or principles on abuse that can be interpreted in accordance with that Article. In light of its answer to that question, the CJEU has not addressed the further questions of the referring court of (1) whether a Danish treaty following Article 10 of the OECD Model[9] and including the expression of BO may constitute a treaty-based anti-abuse provision as referred to in Article 1 (2) of the PSD, and (2) whether BO is to be defined by the national court or is a concept of EU law that must be understood in the same sense as the concept of BO in the IRD, and (3) whether for purposes of interpreting that provision, account is to be taken of Article 10 of the 1977 OECD Model and the Commentary thereto. We will discuss the

[5] Joined cases C-115/15, C-118/16, C-119/16 and 299/16 ('*IRD-case*') and joined cases C-116/16 and C-117/16 ('*PSD-case*').

[6] Art. 1 (2) PSD in its version prior to the amendment by Directive 2015/121 of 27 Jan. 2015. After this amendment, this provision is included in Art. 1 (4) PSD. Because the PSD-case relates to tax years prior to this amendment, we will further refer to Art. 1 (2) PSD.

[7] '*Reservation of competence*' is the term used by the CJEU for such a kind of provision in its judgment of 17 July 1997, C-28/95, *Leur Bloem*, § 39. *See also* P. Wattel, O. Marres & H. Vermeulen, *Terra/Wattel European Tax Law*, volume I, 263 (7th ed., Wolters Kluwer 2018); De Broe, *supra* n. 4, at 996.

[8] CJEU, 26 Feb. 2019, PSD-case, §§ 31–33, IRD-case, §§ 24–26.

[9] A reference to the OECD Model and the OECD Commentary in this contribution is to be understood as a reference to the 2017 version of the OECD Model and its Commentary. If we refer to another version of the OECD Model and OECD Commentary we explicitly included the version.

CJEU's answer to the first question sub 3 and 4 below. The BO related questions are discussed sub 5 below.

In the IRD-case, the CJEU first addressed the meaning of the expression of BO as used in Article 1 (1) and (4) of the IRD.[10] More in particular, the CJEU has been asked (1) how this concept is to be interpreted; (2) whether this concept should be interpreted in accordance with the OECD's BO concept of Article 11 included in the 1977 OECD Model; and, (3) if the answer to the previous question is affirmative, whether solely the Commentary to the 1977 OECD Model should be taken into account or also commentaries to subsequent OECD Models (in particular the Commentary to the 2003 OECD Model and 2014 OECD Model). We will discuss this hereunder sub 5. The CJEU subsequently turned to the questions of the referring court similar to those raised in respect of the PSD and the permitted anti-abuse provisions, but of course linked to Article 5 of the IRD and the notion of BO as included in Danish treaties following Article 11 OECD Model. The CJEU's answer to those questions is the largely same as its answer to the questions raised under the PSD and we will deal with it sub 3 and 4 below.

In case C-118/16, the referring court also asked the CJEU whether a Luxembourg company operated as a SCA (société en commandite par actions) with the status of a SICAR (société d'investissement en capital à risque) is a qualifying company to benefit from the IRD. We will not discuss this question here.

Finally, in both judgments the CJEU also addressed a series of questions from the referring court concerning the interpretation of the freedom of establishment and the free movement of capital in case where an abuse of the PSD or IRD is proven in order for them to establish whether the Danish legislation infringes those freedoms. We will also not discuss these issues here.

3 No need for a specific domestic or treaty-based provision implementing Article 1 (2) of the PSD or Article 5 of the IRD – General principle of EU law that EU law cannot be relied on for abusive purposes

3.1 The Judgments of 26 February 2019

The referring court asked the CJEU whether in order to strike down abuse of the PSD and the IRD, Denmark must have adopted specific domestic or treaty-based anti-abuse provisions referred to in Article 1 (2) of the PSD and Article 5 of the IRD or, if that is not the case, whether it suffices that national law contains general provisions or principles on abuse that can be interpreted in accordance with those Articles. One may have thought that after the CJEU's judgment in *Kofoed*, another Danish abuse-case,[11] this issue is to be considered as '*acte éclairé*'.[12] The *Kofoed*-case concerned a Danish individual who exchanged shares in a Danish company for shares in an Irish company, followed by a dividend distribution by the Danish company. The Danish tax authorities claimed that these transactions abused the 1990 Merger Directive ('*MD*'). In accordance with article 11 (1) (a) of the MD, a Member State may refuse to apply or withdraw the benefits granted under the Directive if the transaction has as its principal objective or as one of its principal objectives tax evasion or tax avoidance.[13] It is settled case law that when a Member State has failed to correctly transpose a Directive into domestic law, it cannot impose obligations stemming from that non-transposed Directive against an individual (principle of 'inverse vertical direct effect' or 'estoppel'[14]), as this would infringe the general EU law principle of legal certainty.[15] As article 11 of the MD was not as such transposed into Danish domestic law, the CJEU nevertheless invited the national court to explore whether Danish law provided for a provision or general principle prohibiting the abuse of rights, which may be interpreted in such a way as to prevent abuse of the MD (so-called directive-compliant interpretation of domestic law to achieve the purpose of the directive).[16] However, as the CJEU observed in its judgment in e.g. *Arcaro*, there are also limits to such directive-compliant interpretation of domestic law. Such limits lie:

[10] The interpretation of the BO requirement for PEs included in Art. 1 (5) of the IRD was not at stake in the IRD-case. Our analysis will therefore be limited to the BO requirement in Art. 1 (4) of the IRD.

[11] CJEU, 5 July 2007, Case C-321/05, *Kofoed*, §§ 41–47.

[12] The acte éclairé-doctrine means that the national court that would normally be under an obligation to submit a question for preliminary reference to the CJEU, may refrain from doing so '*when the question raised is materially identical with a question that has already been the subject of a preliminary ruling [of the CJEU] in a similar case*' (CJEU, 27 Mar. 1963, joined cases 28/62, 29/62 and 30/62, *Da Costa*).

[13] Council Directive 90/434/EEC of 23 July 1990. After the amendment of the MD by Directive 2009/133/EC of 19 Oct. 2009, that provision is now included in Art. 15 of the MD.

[14] The doctrine of inverse vertical direct effect is the opposite of the doctrine of direct effect which was formulated by the CJEU for the first time in its judgment of 19 Jan. 1982, C-8/81, *Becker*, § 25. According to the doctrine of direct effect, when a Member State has failed to implement provisions of a Directive, an individual may rely on the provisions of that Directive against a Member State, provided that such provisions are unconditional and sufficiently precise to set aside any national provisions which are incompatible with the Directive or where the provisions of the Directive accord rights to the individual which he may assert against the State.

[15] CJEU, 8 Oct. 1987, C-80/86, *Kolpinghuis Nijmegen BV*, § 9; CJEU, 5 Apr. 1979, C-148/78, *Ratti*, §§ 22–23; CJEU, 5 July 2007, Case C-321/05, *Kofoed*, § 45 and, more recently, CJEU, 12 Dec. 2013, C-425/12, *Portgás*, § 22.

[16] The judicially developed doctrine imposing the duty on national authorities and courts to interpret the provisions of domestic law as far as possible to achieve the objective pursued by the Directive is based on the principle of EU loyalty (Art. 4 (3) TEU). It is to be seen as one of the exceptions to the principle of estoppel (CJEU, 13 Nov. 1996, C-106/89, *Marleasing SA*, § 6 and, more recently, CJEU, 19 Jan. 2010, C-555/07, *Kücükdeveci*, §§ 47–48; CJEU, 13 Feb. 2014, C-18/13, *Maks Pen*, § 36).

> *where such an interpretation leads to the imposition on an individual of an obligation laid down by a directive which has not been transposed or, more especially where it has the effect of determining or aggravating, on the basis of the directive and in the absence of a law enacted for its implementation, the liability in criminal law of persons who act in contravention of that directives provisions.*[17]

The judgment in *Kofoed* suggests that the transposition of an anti-abuse rule authorized by a Directive into domestic law does not necessarily require legislative action by a Member State, but at least the Member State's general legal context should contain an appropriate measure (i.e. a statutory GAAR or specific anti-avoidance rule (SAAR) or a (judicially developed) principle prohibiting the abuse of rights) that can be interpreted so as to permit that Member State to strike down abuse of the Directive and to deny the taxpayer the benefit pursued under that Directive. If a Member State has failed to transpose the Directive and were to deny the benefit of the Directive to a taxpayer in the absence of an appropriate domestic measure, it would, contrary to the principle of estoppel, aggravate the taxpayer's tax liability.[18]

The judgment in *Kofoed* fits into the settled case law of the CJEU in the area of non-transposition of Directives into domestic law. It is also correct in view of the clear terms of Article 11 (1) (a) of the MD that allow Member States to enact measures preventing abuse of the Directive but do not impose an obligation on them to do so. Member States have reserved their sovereignty in the area of combating tax avoidance under the MD and consequently are free to decide not to do so.[19] However, from a perspective of fairness the *Kofoed*-judgment leads to an unsatisfactory result. Abuse of EU tax law is present (i.e. tax advantages are claimed in a case where it would be inconsistent with the objectives of the Directive to grant those advantages), but that abuse is not struck down.[20]

As Denmark also failed to implement Article 1 (2) of the PSD and Article 5 of the IRD in its domestic law, which like Article 11 (1) (a) of the MD include a reservation of competence by the Member States to enact anti-abuse measures (*see* above sub 1), one would have expected the CJEU to refer to its judgment in *Kofoed* to reach a similar result.

However, that is not what the CJEU decided in the PSD and IRD-cases. In paragraphs 96 to 102 of the IRD-case,[21] referring to a series of earlier judgments, it holds that it is settled case-law that there is in EU law a general principle that EU law cannot be relied on for abusive or fraudulent ends and that that principle must be complied with by individuals. In order to further underscore the general comprehensive character which is naturally inherent in general principles of EU law, the CJEU refers to the fact that it has developed the principle that rights cannot be abused under EU law over a life span of thirty years starting in 1985[22] and in various areas of European law such as the free movement of goods, the freedom to provide services, the freedom of establishment, company law, public service contracts, social security, transport, social policy, restrictive measures, export refunds and VAT.[23] It follows from that general principle that abusive practices are prohibited under EU law and that Member States must rely on that principle against a person who invokes rules of EU law providing for an advantage in a manner that is inconsistent with the objectives pursued by those rules.

It is surprising that the CJEU in the firm statement made in paragraph 96 of its judgment in the IRD-case refers to five cases whereas in three of those the CJEU did not decide on the existence of a general principle of EU law.[24] It is equally remarkable that it fails to mention there the aforementioned *Kofoed*-case (although it is like the PSD- and IRD-cases a direct tax case) which was the first case in which the CJEU recognized that the prevention of abuse is a general principle of EU law. In the long series of cases in which the CJEU dealt with abuse, the first signs of the prevention of abuse qualifying as a general principle of EU law were expressed by the opining advocate general (AG). The first in line was AG La Pergola, whose opinion in *Centros* (1998) (a case of company law which concerned the establishment of a UK company by two Danish residents) held that the prevention of abuse was among the general principles of EU law.[25] Almost seven years later, in

[17] CJEU, 26 Sept. 1999, C-168/95, *Arcaro*, § 42.

[18] De Broe, *supra* n. 4, at 1034.

[19] A. Garcia Prats et al., *EU Report*, in *IFA, Seeking Anti-Avoidance Measures of General Nature and Scope – GAAR and Other Rules*, vol. 103a, 81, 84 & 90 (CDFI 2018); Wattel, Marres & Vermeulen, *supra* n. 7, at 263; D. Weber, *Abuse of Law in European Tax Law: An Overview and Some Recent Trends in the Direct and Indirect Tax Case Law of the CJEU – Part 1*, ET 563 (2013).

[20] De Broe, *supra* n. 4, at 1034.

[21] Similar judgment in CJEU, 26 Feb. 2019, PSD-case, §§ 70–76.

[22] It is remarkable that the CJEU does not refer to the very first case in which it dealt with an alleged abuse of the Treaty freedoms where it held that Member States can take measures to prevent such abuse and which dates back to 1974 (CJEU, 3 Dec. 1974, C-33/74, *Van Binsbergen,* §§ 13–15).

[23] CJEU, 26 Feb. 2019, PSD-case § 74 and IRD-case § 100. The CJEU could have added that it also referred to the principle of abuse of rights in matters concerning the free movement of persons (e.g. CJEU, 17 July 2014, joined cases C-58/13 and 59/13, *Torresi);* the free movement of workers (e.g. CJEU, 21 June 1988, C-39/86, *Lair);* association agreements (e.g. CJEU, 30 Sept. 1997, C-36/96, *Günaydin);* migration law (e.g. CJEU, 23 Sept. 2003, C-109/01, *Akrich* and CJEU, 18 Oct. 2004, C-200/02, *Chen);* tariff quota (e.g. CJEU, 13 Mar. 2014, C-155/13, *SICES* and CJEU, 14 Apr. 2016, C-131/14, *Cervati);* capital duties (e.g. CJEU, 7 June 2007, C-178/05, *Commission v. Hellenic Republic*); common agricultural policy (e.g. CJEU, 14 Dec. 2000, C-110/99, *Emsland Stärke* and CJEU, 3 Mar. 1993, C-229/83, *General Milk*) etc.

[24] In the cases *Centros, Halifax* and *Cadbury Schweppes* the CJEU has not ruled on the general principle. However, it did so in CJEU, 22 Nov. 2017, C-251/16, *Cussens and Others* and the recent case CJEU, 11 July 2018, C-356/15, *Commission v. Belgium* but those are not the first cases in which it characterized its abuse-doctrine as constituting a general principle of EU law.

[25] Opinion AG La Pergola, 16 July 1998, C-212/97, *Centros Ltd*, § 20.

his opinion in *Halifax* (2005) (VAT-case), AG Maduro stated that the prohibition of abuse is an EU principle of interpretation.[26] However, in neither of those cases did the CJEU confirm the positions expressed by the AG. It was only in *Kofoed* (2007) that the CJEU (albeit not the Grand Chamber) ruled for first time that Article 11 (1) (a) of the MD reflects the general principle of EU law that *'abuse of rights is prohibited'*.[27] Over the past years the CJEU confirmed that its doctrine that EU law cannot be relied on for abusive purposes constitutes a general principle of EU law in a number of cases involving VAT,[28] social security[29] and direct tax law.[30]

The judgments in the area of VAT (to which the CJEU frequently refers in the PSD- and IRD-cases) are of particular importance to understand the holdings of the CJEU in those cases. In *Italmoda* (2014) (a case concerning VAT carousel fraud), the CJEU held that it follows from the general principle that no one may benefit from the rights stemming from the European Union's legal system for abusive or fraudulent ends, that it is the responsibility of the national tax authorities and courts to deny advantages fraudulently claimed under the VAT Directive. Referring to its judgment in *Kofoed*, it said that it is for the national court to interpret national law as far as possible and to do whatever lies in its jurisdiction to achieve the objective pursued by the VAT Directive (i.e. the prevention of tax evasion), thereby taking the whole body of domestic law into consideration and applying the interpretative methods recognized by that law. According to the CJEU, the refusal of benefits in such a case does not amount to imposing an obligation on the individual under the VAT Directive (which would be contrary to the principle of estoppel), but it is merely the consequence of the fact that the objective conditions required for obtaining the benefit have, in fact, not been met. From this, the CJEU further concludes that where the domestic law of the Member State does not contain anti-abuse rules that may be interpreted in accordance with the requirements of EU law to prevent the abuse of EU law, the tax authorities and the courts are nevertheless still under an obligation to refuse the benefits fraudulently claimed under the Directive as such a consequence is *'inherent in the system'*. For the same reason, such a refusal is, in the view of the CJEU, not in the nature of a penalty or a sanction.[31] The CJEU later confirmed this judgment in *Cussens* (2017), which concerned a VAT avoidance scheme involving real property.[32]

This case law in the VAT-area raised the fundamental question whether the principles set out by the CJEU in that area would and could be transposed into the area of direct taxation. Apart from the fact that prima facie that case law conflicts with the settled case law on the principle of estoppel as it imposes obligations on Member States to prevent abuse of EU law where the PSD and IRD do not impose such obligations, there are several arguments that can be brought forward against the extension of that case law into matters of direct taxation governed by the PSD and the IRD. VAT is a fully harmonized area of law with the European Union, while direct taxation is not. In cases like *Halifax, Italmoda* and *Cussens* the VAT Directive – although it has the aim of preventing abuse – did not require nor permit Member States to enact anti-abuse rules in connection with rules that were allegedly abused, whereas the PSD and the IRD allow Member State to adopt measures to prevent abuse of those Directives. And finally, *Italmoda* concerns a case of fraud – in which case a Member State does not need to rely on anti-abuse rule to curb down that fraud –, while the Danish PSD- and IRD-cases involve classic examples of a particular form of tax avoidance called Directive shopping (*see* above sub 1). In her Opinion in the *Kofoed*-case, AG Kokott argued that a Member State cannot rely on the general principle of EU law prohibiting abuse of law 'directly' against the taxpayer, clearly suggesting that the Member State can only refuse the benefits wrongfully sought under the Directive if it has transposed the anti-abuse rule authorized by the Directive into domestic law. According to the AG, if a Member State were to be permitted to rely on such a general principle, the harmonization objective of that Directive would be undermined, legal certainty be jeopardized and the principle of estoppel be infringed as in the AG's view that general principle is much less clear than Article 11 of the MD.[33] AG Kokott repeated this proposition in her Opinions in the Danish PSD and IRD-cases.[34]

However, the CJEU has not followed the above arguments and thus also overruled AG Kokott's Opinion. In fact, the CJEU does not distinguish VAT from direct

[26] Opinion AG Maduro, 7 Apr. 2005, C-255/02, *Halifax*, § 91.

[27] Some authors were reluctant to attach importance to the holding of the CJEU in that case as it was not decided by the Grand Chamber which would according to these authors be necessary to give birth to a new general principle (A. Arnull, *What is a General Principle of EU Law*?, in *Prohibition of Abuse of Law: A New General Principle of EU Law* 20 (R. de la Feria & S. Vogenauer eds, Hart Publishing, Oxford University Centre for Business Taxation 2011)). For the contrary view, *see* K. E. Sorensen, *What is a General Principle of EU Law? A Response*, in *Prohibition of Abuse of Law: A New General Principle of EU Law* 25–32 (R. de la Feria & S. Vogenauer eds, Hart Publishing, Oxford University Centre for Business Taxation 2011).

[28] CJEU, 18 Dec. 2014, joined cases C-131/13, C-163/12 and 164/13, *Schoenimport 'Italmoda' et alia*, §§ 43 and 46; CJEU, 22 Nov. 2017, C-251/16, *Cussens and Others,* § 31.

[29] CJEU, 6 Feb. 2018, C-359/16, *Altun and Others,* § 49; CJEU, 11 July 2018, C-356/15, *Commission v. Belgium*, § 99.

[30] CJEU, 26 Oct. 2017, C-39/16, *Argenta Spaarbank*, § 60; CJEU, 7 Sept. 2017, C-6/16, *Eqiom*, § 26; CJEU, 10 Nov. 2011, C-126/10, *Foggia*, § 50.

[31] CJEU, 18 Dec. 2014, joined cases C-131/13, C-163/12 and 164/13, *Schoenimport 'Italmoda' et alia*, §§ 41–62.

[32] CJEU, 22 Nov. 2017, C-251/16, *Cussens and Others*, § 34.

[33] Opinion of AG Kokott, 8 Feb. 2007, C-321/05, *Kofoed*, § 67.

[34] Opinion of AG Kokott, 1 Mar. 2018, C-116/16, *T Denmark*, §§ 99–100 (PSD-case) and in C-115/16, *N Luxembourg 1* (IRD-case), §§ 103–04.

taxation and confirms its case law in *Italmoda* and *Cussens*.

It first holds that whilst Article 1 (2) of the PSD and Article 5 (1) of the IRD provide that the Directive does not preclude the application of domestic or treaty based anti-abuse provisions, such Articles cannot be interpreted as excluding the application of the general principle of EU law that abusive practices by taxpayers are prohibited. Likewise the CJEU rules that Article 5 (2) of the IRD according to which a Member State may withdraw the benefits of that Directive in case of abuse, cannot be interpreted as excluding the application of that general principle since the application of that principle is not subject to transposition in domestic law.[35] Such leads the CJEU to conclude:

> *Thus, in light of the general principle of EU law that abusive practices are prohibited and of the need to ensure observance of that principle when EU law is implemented, the absence of domestic or agreement-based anti-abuse provisions does not affect the national authorities' obligation to refuse to grant entitlement to rights provided for by Directive 2003/49 where they are invoked for fraudulent or abusive ends.*[36]

Of course, the taxpayer relied on the *Kofoed*-case to win suit. However, the CJEU dismissed the taxpayer's arguments. The CJEU starts by recalling what it has decided in *Kofoed*, but then repeats its holding in the VAT-case of *Italmoda*:

> *Nevertheless, even if it were to transpire in the main proceedings, that national law does not contain rules which may be interpreted in compliance with Article 5 of Directive 2003/49, this –* ***notwithstanding what the Court held in the judgment of 5 July 2007 in Kofoed (…)*** *– could not be taken to mean that the national authorities and courts would be prevented from refusing to grant the advantage derived from the right of exemption provided for by Article 1 (1) of the directive in the event of fraud or abuse of rights (see by analogy, judgment of 18 December 2014 in Schoenimport "Italmoda" Mariano Previti and Others (…), paragraph 54)* (authors underline).[37]

And the CJEU adds that refusing the taxpayer the advantage sought under the Directive in cases where he abuses that Directive is not covered by the holding in *Kofoed* since such a refusal is based on the general principle of EU law. In cases of abuse:

> *the refusal of an advantage under a directive (…) does not amount to imposing an obligation on the individual concerned under that directive, but is merely the consequence of the finding that the objective conditions required for obtaining the advantage sought, prescribed by that directive as regards that right, are met formally only (see by analogy, judgment of 18 December 2014 in Schoenimport "Italmoda" Mariano Previti and Others (…), paragraph 57 and the case-law cited).*[38]

[35] CJEU, 26 Feb. 2019, PSD-case § 77, IRD-case §§ 104–05.

[36] CJEU, 26 Feb. 2019, PSD-case § 83, IRD-case § 111.

[37] CJEU, 26 Feb. 2019, PSD-case § 89, IRD-case § 117.

Thereafter, the CJEU clarified when an interposed company abuses the provisions of the PSD and IRD on the withholding tax exemptions in the Member State of source and when Directive shopping becomes illegitimate. We will discuss this part of the judgments sub 4 below. Now we will draw some conclusions and make some observations on the judgments.

3.2 Some Conclusions and Observations on the Judgments of 26 February 2019

3.2.1 Preliminary Remark

There is no doubt that the judgments in the PSD- and IRD-cases have far-reaching consequences all of which we may not oversee today. However, it should be pointed out that their relevance for the issue discussed here (i.e. the absence of appropriate anti-abuse measures in domestic law) will become less important in future years. In 2015 the PSD has been amended and supplemented with a mandatory GAAR (Article 1 (2) and (3) of the PSD),[39] leaving no discretion to Member States anymore as to the prevention of abuse under the PSD. And as of 1 January 2019, all Member States should, pursuant to Article 6 of Anti Tax Avoidance Directive ('*ATAD*'), have enacted a GAAR that operates in the field of corporate taxes, both in domestic and cross-border transactions.[40] As withholding taxes are in most Member States a technique to levy corporate tax and the levy of withholding tax in case of non-resident corporation is often a final levy of corporate tax in the State of source of the income, it is submitted that – unless clear indications to the contrary in the domestic laws of the Member State – any abuse of withholding taxes on dividends, interest and royalties by non-resident companies come within the scope of the ATAD GAAR.[41]

3.2.2 Kofoed *overruled?*

The CJEU has pulled the emergency break and shut the door for the abuse of direct tax Directives which was left

[38] CJEU, 26 Feb. 2019, PSD-case, § 91, IRD-case § 119.

[39] As amended by Directive 2015/121. Art. 1 (2) now reads as follows: '*Member States* ***shall not grant*** *the benefits of this Directive to an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of this Directive, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one strep or part*' (authors underline). Art. 1 (3) clarifies that '*For the purposes of paragraph 2, an arrangement or a series of arrangements shall be regarded as not genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality*'. Art. 1 (2) that was at stake in the PSD-cases that we discuss here has since then become Art. 1 (4) of the PSD.

[40] Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market.

[41] L. De Broe & S. Gommers, *Art. 29: Entitlement to Benefits (European Union) – Global Tax Treaty Commentaries*, Global Topics IBFD (accessed 26 Aug. 2019).

open after its *Kofoed*-judgment. Case law in matters of harmonized VAT law and in matters of harmonized direct tax law (PSD, IRD and MD) has now converged. We believe that this was the intention of the CJEU (see the three references in the PSD and IRD-judgments to the analogy with the decision in the VAT-cases of *Italmoda* and the references to the judgment in *Cussens*[42]) and that this is a logic development. As its judgments are based on the existence of a general principle of EU law that abuse of rights stemming from EU law is to be prevented and one can hardly imagine how the application of that principle could be different from one area of tax law to the other. We therefore do not believe as a group of authors suggests that the judgments can be explained by the way in which Denmark had transposed the provisions of the Directive into its domestic law which may be read as importing all criteria of the Directives (including the general principle on the prohibition of abuse of rights) in domestic law.[43] The references to the absence of appropriate anti-abuse measures in Danish law in paragraphs 31 to 33 of the judgments in the PSD-case and paragraphs 24 to 26 in the IRD-case, make it clear that in the eyes of the CJEU Denmark had not transposed Article 1 (2) PSD, nor Article 5 IRD in its domestic law.[44] The judgments only make sense against that background. Had there been some transposition the CJEU could have simply referred to its *Kofoed*-judgment.

In the authors' view the CJEU has refined – and in light of the wording *'notwithstanding what the Court held in the judgment of 5 July 2007 in Kofoed'* in paragraph 89 of the PSD-judgment and paragraph 117 of the IRD-judgment one may say overruled[45] – its holding in *Kofoed*. The case law as stands today after the recent VAT-, PSD- and IRD-cases goes well beyond the *Kofoed*-judgment. It follows from the CJEU's recent judgments in these cases that it is an unwritten condition for a taxpayer to claim benefits under a Directive that he does not abuse the provisions of the Directive that provide for such benefits. Denying the taxpayer the benefits sought under the Directive where abuse is established does not amount to imposing an obligation onto the taxpayer, which a Member State that has failed to transpose the Directive would otherwise be unable to do under the settled case law on 'estoppel'. It is the mere consequence of the taxpayer failing to meet the conditions required for rightfully obtaining those benefits. Where in *Kofoed*, the CJEU (first chamber) decided that the general EU law principle that abuse is prohibited, requires the national court to explore what it can do to that effect under (the interpretation of) its national law, the Grand Chamber of the CJEU now decides that even if there is no such possibility under national law, the competent authorities of the Member States must at all times prevent taxpayers from abusing the provisions of a tax Directive. Consequently, the tax authorities and courts of a Member State should refuse the benefits claimed by a taxpayer under that Directive if he acts abusively, even if that Member State has not transposed the mandatory or optional anti-avoidance rule included in the Directive into its domestic law and even if the Directive itself would not provide for an anti-abuse rule altogether, provided, however, that the Directive (like the VAT Directive) has the clear objective of preventing tax abuse.[46] Hence, a cynical may now ask why the PSD and the ATAD do provide for a GAAR?

In light of the above, we submit that the Grand Chamber of the CJEU has intentionally overridden *Kofoed* and aligned the case law in the area of harmonized direct taxation to the case law in the area of VAT[47] with the aim to avoid that Member States would be unable to curb down cases where abuse of direct tax and VAT Directives is established.

Abuse thus operates as an unwritten exception to the enjoyment of benefits under a (tax) Directive. It comes into motion after it has been established, first, that the taxpayer formally meets the conditions for enjoying those benefits and, secondly, that the taxpayer wrongfully claims those benefits, i.e. against the purpose for which those benefits have been conceived. This follows clearly from the double test which the CJEU has developed to establish an abuse of EU law (*'despite formal observance of the conditions laid down by the EU rules, the purpose of these rules has not been achieved'; see* below sub 4.1.), from paragraphs 91 of the judgment in the PSD-case and paragraph 119 of the judgment in the IRD-case and from specific holdings of the CJEU and opinions of AG's in other cases.[48] That explains why the CJEU can say that refusing the benefit of the Directive, even if the Member State has not transposed Article 1 (2) of the PSD or Article 5 of the IRD in its domestic law and thus does not provide for an appropriate anti-abuse measure, is not the same as imposing an obligation onto a taxpayer under a non-transposed Directive.

[42] CJEU, 26 Feb. 2019, PSD-case §§ 76, 89, 90 and 91, IRD-case §§ 102, 105, 117 and 119.

[43] CFE, *Opinion Statement ECJ-TF 2/2019 on the CJEU decisions of 26 Feb. 2019 in Cases C-115/16, C-118/16, C-119/16 and 299/16, N Luxembourg I et al, and Cases C-116/16 and 117/17 T Denmark et al, concerning the 'beneficial ownership' requirement and the anti-abuse principle in the company tax directives*, 14 and 16.

[44] Also: D. Leczykiewicz, *Prohibition of Abusive Practices as a 'General Principle of EU Law'*, Com. Mkt. L. Rev. 740 (2018).

[45] G. F. Boulogne, *Interestbetalingen tussen lidstaten: verplichting om misbruik te bestrijden en uitleg als uiteindelijk gerechtigde*, 53(8) FED 52 (2019).

[46] CJEU, 22 Nov. 2017, C-251/16, *Cussens and Others*, § 28.

[47] It is important to note that the VAT-cases were not decided by the Grand Chamber. *Italmoda* was decided by the 1st Chamber and *Cussens* by the 4th Chamber.

[48] *See* e.g. CJEU, 6 Apr. 2006, C-456/04, *Agip Petroli*, § 23; CJEU, 6 Nov. 2003, C-413/01, *Ninni-Orasche*, § 31; Opinion of AG Sanchez-Bordona, 4 Dec. 2018, C-621/18, *Wightman et alia v. Secretary of State for Exiting the European Union*, § 152. *See also* Sorensen, *supra* n. 27, at 26; L. van Hulten & J. Korving, *Svig og Misbrug; The Danish Anti-Abuse Cases*, Intertax 795 (2019).

3.3 Is the Prohibition to Abuse of Rights Under EU Law, a General Principle of EU Law? And if so, What Is the Consequence Thereof?

Within its mission to ensure that in the interpretation and application of the Treaties, the law is observed (Article 19 (1) TEU), the CJEU has regularly had recourse to general principles in interpreting and applying EU law (e.g. principles of equality, legal certainty, proportionality). These principles form part of the Union legal order and infringement of them constitutes '*an infringement of the Treaties or of any rule of law relating to their application*' (Article 263, second paragraph TFEU). The CJEU applies principles that it finds, if not expressly, at least implicitly in the legal traditions of the Member States, but it often recognizes general principles of law as forming part of the EU legal order without expressly referring to the constitutional traditions of the Member States. The CJEU typically puts forward a general principle where it is impliedly associated with the concepts applied by the Member States.[49] The fact that a principle is not universally recognized in the national laws of the Member States does not prevent the CJEU from lifting it to the level a general principle of EU law if there were sufficient support for such development in the national systems of the Member States and it is considered conducive to the proper functioning of the Union's legal order.[50]

There are several reasons why we agree with the CJEU that in its case law as its stands today the principle of the prohibition of abuse of rights has achieved the status of a general principle of Union law.[51] First, although the CJEU did not engage in a discovery whether the principle is common to the laws of the Member States, the concept of abuse of rights is known in the laws of several Member States and most of the Member States have recourse to GAARs and SAARs or judicially developed doctrines to strike down cases of abuse of rights in matters of impermissible tax avoidance. Additionally, since the ATAD, every Member State should adopt a GAAR in its domestic laws to prevent abuse of its rules of corporate tax law (*see* above sub 3.1.).[52] Secondly, since the mid-1970s, the CJEU has issued a long series of judgments in various fields of law that contributed to the development of the EU concept of abuse of rights.[53] Third, the general EU law principle of the prohibition of abuse meets several of the functions which are typically asserted to general principles of EU law.[54] First, it operates as an aid to the interpretation of EU law. Provisions of EU law are to be interpreted as requiring the denial of a right, where although the formal conditions for claiming that right are met, the exercise of that right would be abusive. In other words, EU law should not be interpreted in a way that promotes or facilitates abuse of that law. Second, it operates as a gap filler to safeguard the coherence of EU law, i.e. the integrity and effectiveness of EU law would be undermined if abuse of that law would not be curtailed.[55] In doing so, the principle achieves harmonization of the fight against tax fraud and tax avoidance within the EU where tax law has been harmonized (VAT, PSD, IRD and MD). In view thereof, we believe that the abuse concept as developed by the CJEU over a time span of forty years now possesses the general, comprehensive character which is otherwise naturally inherent in other general principles of law.[56] And we agree with Vogenauer who concluded (already in 2011) that the CJEU developed the principle in an intuitive fashion on the basis of a tacit understanding of the nature and the application of the rules of EU law which assumes that any legal order needs '*self-protection measures*' or '*safety valves*' to ensure that the rights it confers are not exercised in a manner which is abusive, excessive or distorted.[57]

It is observed that the general principle of prohibition of abuse of EU law is of a particular nature when compared to the other general principles recognized by the CJEU (e.g. non-discrimination, proportionality, legal certainty). As a rule, the general principles of EU law bind the institutions of the EU and the Member States. They are measures to control the legality of acts of such institutions and Member States that affect the rights of private parties. Hence, they serve to protect the rights enjoyed by private parties under EU law. The general principle that

[49] K. Lenaerts & P. Van Nuffel, *European Union Law*, Sweet & Maxwell 851 et seq. (2011).

[50] Arnull, *supra* n. 27, at 18.

[51] Before the decisions in the VAT-cases and the PSD- and IRD-cases, it has been heavily debated whether the concept of abuse of rights as developed in the CJEU's case law, could be constituting a general EU law principle. *See* e.g. Contra: Arnull, *supra* n. 27, at 20–23; *See* e.g. Pro: Sorensen, *supra* n. 27, at 25–32; Lenaerts & Van Nuffel, *supra* n. 49, at 857; A. Lenaerts, *The General Principle of the Prohibition of Abuse of Rights: A Critical Position on Its Role in a Codified European Contract Law*, Eur. Rev. Priv. L. 1139 (2010). Nuanced: L. De Broe & D. Beckers, *The General Ant-Abuse Rule of the Anti-Tax Avoidance Directive: An Analysis Against the Wider Perspective of the European Court of Justice's Case Law on Abuse of EU Law*, EC Tax Rev. 136–39 (2017).

[52] For a thorough analysis of the existence of a principle of abuse or rights in the domestic laws of the Member States, *see* Lenaerts, *supra* n. 51, at 1121–54.

[53] *See* the cases cited by the CJEU in PSD-case § 74 and the IRD-case § 100 and the cases cited in footnote 23.

[54] K. Lenaerts & J. A. Guttiérrez-Fons, *The Constitutional Allocation of Powers and General Principles of EU Law*, Com. Mkt. L. Rev. 1629 (2010); T. Tridimas, *General Principles of EC Law*, Oxford L. Lib. 29 et seq. (2006).

[55] Sorensen, *supra* n. 27, at 26–27.

[56] CJEU, 22 Nov. 2017, C-251/16, Cussens, § 31; CJEU, 15 Oct. 2009, C-101/08, *Audiolux*, § 42.

[57] S. Vogenauer, *The Prohibition of Abuse of Law: An Emerging General Principle of EU Law* in *Prohibition of Abuse of Law: A New General Principle of EU Law* 570 (R. de la Feria & S. Vogenauer eds, Hart Publishing, Oxford University Centre for Business Taxation 2011). The author cites the Opinions of AG Tesauro of 4 Dec. 1998 in C-367/96, *Kefalas*, § 24 and AG Maduro of 7 Apr. 2005 in C-255/02, Halifax, § 74. Note that even after the judgments in *Cussens* and the *PSD- and IRD-cases*, authors continue to contest on doctrinal grounds that the prohibition to abuse EU law constitutes a general principle of EU law enforceable against private parties, *see* Leczykiewicz, *supra* n. 44, at 703–42, in particular at 734 & 741.

EU law cannot be abused, however, is a principle that should be respected by private parties and that can and should be enforced as against such parties in case they abuse EU law.[58] On the other hand, AG's have recently opined that nothing excuses Member States from not respecting that same general principle when they exercise powers (e.g. legislative powers) that affect the rights of subjects of law.[59]

If the prohibition of abuse of EU law has become a general principle of EU law, the national authorities of the Member States must respect such principle, regardless whether their powers are legislative, executive, administrative or judicial.[60] They then have a duty to prevent abuse of EU law under the terms of such principle and they derive from EU law an autonomous legal ground for doing so, even if there is no adequate legal basis in their national law to comply with that duty.[61] There are several reasons supporting that position, the most important being the principle of loyal cooperation (Union loyalty, Article 4 (3) TEU) which requires Member States to take any appropriate measure to ensure the fulfilment of the obligations arising from the Treaty or resulting from the acts of the institutions of the European Union.[62] Accordingly, as the prohibition of abuse is a general principle of EU law, the CJEU is correct to conclude that a Member State does not need a legal basis in domestic law to prevent that abuse as it derives that basis directly from EU law itself.

3.4 Another Blow for the Sovereignty of the Member States in the Area Taxation, a Play With Constitutional Fire or an Infringement of the Principle of Legal Certainty?

The above, however, does not mean that the CJEU's judgments in the PSD- and IRD-cases do not give rise to fundamental observations.

These judgments are a serious blow for the sovereignty which Member States have intentionally reserved for themselves under Article 1 (2) of the PSD and Article 5 of the IRD. Member States intended to decide freely whether they would take measures preventing abuse of the PSD and IRD and, if they have adopted such measures, to decide on their form. The recent case law of the CJEU has made clear that this was an illusion. In particular with respect to measures preventing abuse of the PSD, the CJEU has in a first step, recently held that these measures (taking the form of irrebuttable presumptions of abuse or presumptions based a series of predetermined general criteria of abuse) had disproportional effects because they targeted non-abusive cases or, where they used discriminatory criteria, infringed the fundamental freedoms and had therefore to be disapplied.[63] With the judgments in the PSD- and IRD-cases discussed here, the CJEU has gone one step further and decided that Member States that have not taken any measure to prevent abuse of the Directives, still have an obligation to strike down that abuse. Consequently, it has now become clear that the reservations of competence in the various direct tax Directives (PSD, IRD and MD) do not offer a free choice to the Member States and that they are completely redundant. Another instrument of tax competition (i.e. one Member State being more taxpayer friendly in the enforcement of Directives than another) has been eliminated. Such reservations of competence should be deleted from the PSD, IRD and MD and where necessary be replaced by a mandatory GAAR, as is now the case for the PSD.

This conclusion does not sit easily with the fact that the PSD and IRD only provide for minimum harmonization as is clearly illustrated by the optional language in which Article 1 (2) of the PSD and Article 5 of the IRD are couched. These provisions leave a wide margin of discretion to the Member States. The judgments therefore seriously interfere with the powers which Member States have intentionally retained. Authors commenting on the judgments in the PSD- and IRD-cases have therefore written that *'A different understanding would be quite a blow against the domestic separation of powers in that it undermines the decision of a national legislator not to*

[58] Tridimas, *supra* n. 54, at 48. The author writing in 2006 therefore questioned whether general principles could impose obligations on individuals and was of the opinion that the CJEU was reluctant to recognize general principles that may by themselves impose obligations on individuals. Also: Arnull, *supra* n. 27, at 20. But cf. to Vogenauer, *supra* n. 57, at 566 writing in 2011: '*There is no reason why a general principle should never give rise to obligations against private persons, as long as the necessary safeguards apply and the rule of law is observed*'.

[59] It was formulated for the first time by AG Sanchez-Bordona in the case concerning the notification of the UK and Northern Ireland to withdraw from the EU (Opinion of AG Sanchez-Bordona of 4 Dec. 2018, C-621/18, *Wightman et alia v. Secretary of State for Exiting the European Union*, §§ 153 & 170). *See also* Opinion of AG Kokott of 13 June 2019 in C-75/18, *Vodafone Magyarorszag Mobil Tavközlesi*, § 88.

[60] J. Temple Lang, *The Sphere in Which Member States Are Obliged to Comply With General Principles of Law and Community Fundamental Rights Principles*, L.I.E.I., 30–33 (1991). *See* e.g. CJEU, 15 June 2006, C-28/05, *G.J. Dokter et alia*, § 74: '*It is equally settled case law that respect for the rights of defence is, in all proceedings initiated against a person which are liable to culminate in a measure adversely affecting that person, a fundamental principle of Community law which must be guaranteed even in the absence of any rules governing the proceedings in question*'.

[61] M. Lang, *Cadbury Schweppes' Line of Cases from the Member States' Perspective*, in *Prohibition of Abuse of Law: A New General Principle of EU Law* 451 (R. de la Feria & S. Vogenauer eds, Hart Publishing, Oxford University Centre for Business Taxation 2011).

[62] De Broe, *supra* n. 4, at 831. AG Kokott in her Opinion in C-75/18 *Vodafone Magyarorszag Mobil Tavközlesi*, § 88 also cites Art. 4 (3) TEU as the legal basis for her conclusion that also Member State are bound to the EU law abuse of rights principle.

[63] CJEU, 7 Sept. 2017, C-6/16, *Eqiom and Enka*, §§ 30 et seq. and CJEU 20 Dec. 2017, joined cases C-504/16 and 613/16, *Deister Holding and Juhler Holding*, §§ 59 et seq. There is similar case law under the reservation of competence in Art. 11 (1) of the former MD, *see* e.g. CJEU, 17 July 1997, C-28/95, *Leur-Bloem*, §§ 41 et seq. *See also* Wattel, Marres & Vermeulen, *supra* n. 7, at 268–74; Garcia Prats et al., *supra* n. 19, at 80–83.

implement an anti-abuse reservation by granting unelected tax officials and judges the power to override that decision based on an EU principle'.[64] Several years ago, similar criticisms have already been formulated in legal doctrine and by AG's after the CJEU's decision in 2005 in *Mangold* (a non-tax-case in which the CJEU interpreted obligations of the Member States under Directive 2000/78 on the basis of the general law principle of non-discrimination as going well beyond the text of the Directive).[65] For example Prechal (now judge at CJEU) observed:

> *In that respect and arguably also due to a not very well articulated reasoning in Mangold, it was feared that by using general principles of law, the ECJ would widen the scope of the directives, bypass democratic decision-making and indirectly also the division of powers between the Union and the Member States (…) It is somewhat difficult to understand that where the Member States are explicitly given certain latitude by a directive, this can be overruled by virtue of a general principle of law.*[66]

The author therefore asks the question: '*So, was the ECJ* [in Mangold, authors' addition] *playing with constitutional fire?*'

This question is of course very pertinent in tax matters. Indeed, under the Constitution of some Member States taxes can only be assessed if the assessment has a basis in rules of law that have been approved by the national Parliament (e.g. Article 170 of the Belgian Constitution (principle of legality)). If a Member State has not enacted a measure that aims at preventing abuse of the EU directives in the field of tax law, but is forced to apply the EU law general principle to prevent such abuse, an argument could be made that the ensuing tax assessment infringes the constitutional rule.[67] That explains, e.g. why in the aftermath of the CJEU's judgment in *Halifax* (requiring the UK to prevent abuse of the VAT Directive even where the Directive did not impose an obligation on the Member States to adopt measures against the abusive exercise of the right to deduct upstream VAT) Belgium decided to enact a GAAR in its VAT Code (Article 1 (10) Belgian VAT Code). It remains to be seen how, in the absence of such a GAAR, the potential conflict between the EU law general principle and the Constitution is to be resolved by the Member State in question.[68]

Although the judgments in the PSD- and IRD-cases are based on the existence of a general principle of EU law that abuse is prohibited, they also raises questions on how they relate to other general EU law principles, in particular the principles of legal certainty and of legitimate expectations. The principle of legal certainty implies that those subject to the law must be able to know the full extent of their rights and obligations under EU law when they plan their actions. Observance of the principle of legal certainty is, as has been stressed by the CJEU in the *Halifax*-judgment, all the more important in the case of rules, such as rules of tax law, that entail financial consequences for the subjects of law.[69] The CJEU has traditionally cited that general principle of legal certainty as the justification for the construction of its doctrine of '*estoppel*' (*see* above sub 2). It is the solid ground for the CJEU's settled case law that a Directive cannot by itself and without national implementation impose obligations on individuals or aggravate their criminal or tax liability when they act contrary to the provisions of that non-transposed Directive. In addition, the general EU law principle of legitimate expectations (which is a particular expression of the principle of legal certainty) implies that those subject to the law may expect from public authorities that they exercise their powers over a period of time in such a way as to ensure that situations and relationships lawfully created under EU law are not affected in a manner which a diligent person could not foresee.[70]

A taxpayer may have set up transactions from a particular Member State (in casu Denmark) – rather than from another Member State – because he has been advised that that first Member State had not adopted anti-abuse measures under the PSD or IRD, whereas other Member States did. Indeed, seen from that perspective, the non-adoption of anti-abuse measures is just another tool in the battlefield of the tax competition between Member States. Arguably, that taxpayer derived from the provisions of the PSD and IRD, the Danish legislation and the CJEU's case law on the principle of 'estoppel' as they stood when he executed the transactions, a legitimate expectation that the Danish tax authorities would not be in a position to successfully argue that these transactions could be qualified as abusing the

[64] W. Haslehner & G. Kofler, *Three Observations on the Danish Beneficial Ownership Cases*, Kluwer Int'l Tax Blog (13 Mar. 2019), http://kluwertaxblog.com/2019/03/13/three-observations-on-the-danish-beneficial-ownership-cases/.

[65] CJEU, 22 Nov. 2005, C- 144/04, *Mangold*. The Directive was based on Art. 13 EC (now Art. 19 TFEU). Although it did not prohibit any form of discrimination Art. 13 EC empowered the Council, within certain limits to take appropriate action to combat discrimination based on sex, racial or ethnic origin, religion or belief, disability, age or sexual orientation. Directive 2000/78 laid down a general framework on some of those grounds, including age. Although the deadline for implementation had not been reached – which is an absolute obstacle for claiming direct effect by an individual – the CJEU ruled that the observance of the general EU law principle of non-discrimination on grounds of age could not be conditional on the expiry of the deadline for the Directive and that it was the responsibility of the national court to guarantee the full effectiveness of that general principle setting aside any contrary national provision.

[66] S. Prechal, *Competence Creep and General Principles of Law*, 3(1) Rev. Eur. Admin. L. 16–17 (2010).

[67] A. Zalasinski, *The ECJ's Decisions in the Danish 'Beneficial Ownership' Cases: Impact on the Reaction to Tax Avoidance in the European Union*, 4 Int'l Tax Stud. 17 (2019).

[68] *See* for Belgium: L. De Broe, *The Belgian Rule Against Abusive Practices in VAT Matters*, in *A Vision of Taxes Within and Outside European Borders* 137 et seq. (L. Hinnekens & P. Hinnekens eds, Festschrift in Honor of Prof. Dr Frans Vanistendael, Wolters Kluwer 2008)

[69] CJEU, 21 Feb. 2006, C-255/02 *Halifax*, § 72.

[70] Opinion of AG Cosmas in C-63/93, *Duff*, § 25.

provisions of the PSD or IRD and to subject him to Danish withholding taxes.[71] The CJEU's holding in the PSD- and IRD-cases is arguably at odds with these principle of legal certainty and legitimate expectations.[72] However, the CJEU's message in the PSD- and IRD-cases is clear. A tax abuser does not deserve protection from the general EU law principles of legal certainty and legitimate expectations.[73] One sees a hierarchy developing in the CJEU's case law. In the area of abuse of Directives, the general EU law principle on the prohibition of abuse prevails over these two other general principles.

In this respect, it is recalled that in our opinion the CJEU's judgments in the PSD- and IRD-cases override the CJEU's case law as it stood after *Kofoed* (*see* above sub 3.2). It is to be noted that it is also settled case law of the CJEU that where a transaction was carried out before a change in the CJEU's case law, the principles of legal certainty, legitimate expectations and non-retroactivity do not prohibit a retrospective application of the change in the CJEU's case law. Indeed, the CJEU has ruled at several occasions that the interpretation which it gives by virtue of Article 267 TFEU, to EU law clarifies and defines the meaning and scope of that law as it must be or ought to have been understood and applied from the date of its entry into force. It follows that, unless truly exceptional circumstances, EU law must be applied by national courts even to legal relationships which arose and were established before the CJEU's holding.[74] Also here there seems to be no room for the principles of legal certainty and legitimate expectations to apply. Accordingly, transactions carried out before the date of the judgments in the PSD- and IRD-cases that are found to have abused the provisions of the PSD or IRD ought to be governed by the principles set out in the CJEU's judgments of 26 February 2019.

From the foregoing it follows that the aforementioned case law should be reserved for cases where the CJEU interprets existing provisions of EU law. In the case at hand, however, it could be argued that the CJEU has developed a new rule of law when it decided that its abuse-doctrine has reached the level of a general principle in (direct) tax matters to which its case law on interpretations given by virtue of Article 267 TFEU is not applicable. In other words, it could be argued that the emergence of a general principle of EU law does not qualify as a clarification of EU law in the sense of this case law. Such a new rule should not, if one wants to respect the principle of legal certainty, be applied to transactions carried on before that date. A subsequent question would then be when that new rule (i.e. the general principle) was born and from which moment transactions can be caught by it. In our view, that can at earliest have been in 2007 with the CJEU's judgment in *Kofoed.* However, as there the CJEU did not open the door for the enforcement of the principle without legal basis in national law, arguably the date of birth is the 2014 *Italmoda*-judgment, or, as this is a fraud case that needs to be distinguished, from a tax avoidance scheme like in the PSD- and IRD-cases, the 2017 judgment in *Cussens* (*see* above sub 3.1).[75]

3.5 What Are the Ramifications of the Existence a General Principle of EU Law on the Prohibition of Abuse for Fighting Tax Avoidance in Matters of Direct Taxation?

In order to determine the function of the general EU law principle that abuse of EU law is to be prevented, we distinguish cases of harmonized tax law from cases of non-harmonized direct tax law.

It is clear that, in matters of harmonized direct tax law (the PSD, the IRD and the MD), Member States no longer have any latitude to prevent abuse of the Directives, notwithstanding their reservations of competence. Tax authorities and courts of Member States should refuse the benefits of the Directives where the taxpayer abusively relies on these Directives, even where the Member State has failed to transpose the optional anti-abuse rules provided for by the Directive into its domestic law.[76] As said above sub 3.4, they should also do so where the transaction was carried out before the change in the CJEU's case law. Of course, in the absence of a domestic anti-abuse measure transposing the rule of the Directive, there is a fair risk that Member States will misapply the general principle of EU law that abuse of EU law is prohibited and in particular the tests developed by the CJEU to determine whether there is an abusive practice (*see* below sub 4) and/or rely on

[71] According to a Danish author certain assurances were given by the Danish Ministry of Taxation when Denmark introduced withholding tax (*see* above sub 1) that Danish tax authorities would not be able to tackle interposed conduits established in other EU Member States that upstream the income to tax havens (Hansen, *supra* n. 1, at 537 et seq. (translation)).

[72] AG Mazak in his Opinion of 15 Feb. 2007 in C-411/05 *Palacios de la Villa* § 138 criticized the CJEU's judgment in the *Mangold*-case for allowing an unjustified interference of EU law with an area of law where the Member States had retained their competence and also argued that the CJEU's holding raised '*serious concerns in relation to legal certainty*'.

[73] One may have read this conclusion already implicitly in the writings of the President of the CJEU: '*EU law does not offer a shield to tax evaders, since Member States may prevent taxpayers from obtaining tax advantages resulting from "wholly artificial arrangements" which do not involve the genuine exercise of an economic activity. Those arrangements constitute abusive practices*' (K. Lenaerts, *The Concept of 'Abuse of Law' in the Case Law of the European Court of Justice on Direct Taxation*, Maastricht J. Eur. & Comp. L., vol. 22, 350 (2015)).

[74] CJEU, 22 Nov. 2017, C-251/16, *Cussens and Others,* §§ 40–41 and the case law cited there.

[75] Leczykiewicz, *supra* n. 44, at 737.

[76] Where the Member State law's include a GAAR or SAAR or judicially developed anti-abuse principle, the latter have to interpreted and applied in a way which is compliant with the Directive and the general principle of abuse of rights as developed by the CJEU in e.g. *Kofoed, Italmoda, Eqiom* and *Deister* quoted above and the PSD- and IRD-cases.

discriminatory or disproportional criteria to refuse tax benefits provided by the Directive (e.g. where the source State of the dividend denies the withholding tax exemption solely because the EU parent company is held by non-EU shareholders). In that case, the CJEU will again be called upon to bring the tax authorities back on track.

The situation is less clear in matters of non-harmonized direct tax law (personal income tax and most areas of corporate income tax before the entry into force of the ATAD GAAR). In matters where the taxpayer allegedly abuses domestic tax law but does not rely on a provision of EU law (for example a purely domestic transaction where the taxpayer does not make use of any fundamental freedom), it clearly follows from the *3M Italia* judgment that the national authorities and courts have no obligation to strike down that abuse on the basis of the general principle of EU law, because EU law is not at stake.[77] In *3M Italia*, the CJEU ruled that no such thing exists as a general principle in EU law that might entail an obligation of a Member State to combat abusive practices in the field of direct taxation where the taxpayer did not make use of a provision of EU law for abusive purposes.[78] Thus prima facie the judgment in *3M Italia* conflicts with the judgments in the PSD- and IRD-cases. *3 M Italia* was about an Italian tax amnesty law that enabled taxpayers to buy off pending tax litigation. The Italian Supreme Court made a request for a preliminary ruling because doubts were raised on whether it is permissible to apply the Italian tax amnesty law in the case of alleged abuse by the taxpayer of the Italian corporate tax rules. It was disputed whether the Italian tax amnesty law was compatible with the prohibition of the abuse of rights as it had been defined by the CJEU in *Halifax* and *Part Service*[79]; two cases, however, that relate to the sphere of harmonized VAT-law. Because the abuse of EU law was not at stake and the Italian tax amnesty law did not restrict the exercise of the EU Treaty freedoms by the taxpayer, the CJEU ruled that the principle of the prohibition of abuse of rights could not prevent the application of that law.

In matters of non-harmonized direct tax law where the taxpayer relies on a provision of EU law (e.g. where he uses a Treaty freedom to circumvent an unfavourable rule of his home Member State and takes advantage of more beneficial tax treatment offered by another Member State), the CJEU's decisions in the PSD- and IRD cases have complicated things. On the one hand, Member States have preserved their sovereignty in that area and thus remain fully competent to organize their domestic tax law. The prevention of tax avoidance is a matter of public interest of each Member State and it is within the Member States' discretion to decide whether and how they will combat tax avoidance strategies that impact their budgets and the integrity of their domestic tax laws, even if EU law is the tool used to circumvent national tax law.[80] Of course, if Member States make use of their domestic anti-avoidance rules or judicial principles, they must do so in accordance with the requirements set by EU law and only target structures that are abusive in the meaning of the CJEU case law (*see* below sub 4) with non-discriminatory and/or proportionate measures within the meaning of the CJEU's case law.[81]

The terms of paragraph 83 of the judgment in the PSD-case and paragraph 111 of the judgment in the IRD-case seem to suggest that the CJEU's holding is limited secondary EU law:

> *Thus, in light of the general principle of EU law that abusive practices are prohibited and of the need to ensure observance of that principle when EU law is implemented, the absence of domestic or agreement-based anti-abuse provisions does not affect the national authorities' obligation to refuse to grant entitlement to rights provided for by [Directive 90/435/ Directive 2003/49] where they are invoked for fraudulent or abusive ends'*.[82]

The CJEU thus reserves the application of the general EU law principle where '*EU law is implemented*'.[83] Although implementation of EU law is, according to the CJEU's case law, a broad notion covering the transposition of a Directive in domestic law, adoption of measures to give effect to a Regulation, application of provisions of EU law and enforcement of EU law, that is not what is at stake here, i.e. the alleged abuse of primary EU law by a taxpayer to enjoy more beneficial tax treatment in another Member State.

On the other hand, although the recent case law of the CJEU concerns harmonized tax law (VAT and direct taxes), these judgments are couched in such general terms that it could reasonably be argued that they apply '*Union-wide*'. The CJEU's judgment in *Cussens* is very illustrative in this respect: '*[…] it is apparent from the Court's case law that the principle that abusive practices are prohibited is applied to rights and advantages provided for by EU law irrespective of whether those rights and advantages* ***have their basis in the***

[77] Also: Zalasinski, *supra* n. 67, at 17.

[78] CJEU, 29 Mar. 2012, C-417/10, *3M Italia SpA*, §§ 30–32.

[79] CJEU 21 Feb. 2008, C-425/06, *Part Service*.

[80] Writing before the judgments in the PSD- and IRD-cases; De Broe, *supra* n. 4, at 832 and Weber, *supra* n. 19, at 263.

[81] De Broe & Gommers, *supra* n. 41.

[82] Of course, one may object that as the CJEU in the PSD- and IRD-cases dealt with secondary EU law, it is logic that it limits its decision to cases where secondary EU law is implemented.

[83] There are two other areas where general EU law principles need to be respected. The first one applies where a Member State adopts a measure under an express TFEU derogation (public policy e.g.) which is not relevant here. The second one applies where '*the measure otherwise falls within the scope of EU law*', which is difficult to grasp and seems to require some connection between the national measure at stake and EU law. Arguably, as in the case discussed here the Member State does not rely on a national anti-abuse measure but denies TFEU access directly on the basis of the general principle prohibiting abuse, that category is not relevant either. For further readings, *see* Prechal, *supra* n. 66; Tridimas, *supra* n. 54, at 36–42.

***Treaties** […], in a regulation […] or in a directive […]'* (authors underline).[84] Accordingly, it stands to reason that the CJEU's case law in harmonized tax law could also apply where a taxpayer makes use of provisions of primary EU law (namely the fundamental freedoms) against their objectives with the mere or predominant purpose of escaping from cumbersome tax provisions of a Member State (a so-called wholly artificial arrangement).[85] The principle of Union loyalty requiring Member States to take appropriate measures to ensure the fulfilment of their obligations arising from the Treaty and from the acts of the EU institutions (Article 4 (3) TEU) and the fact that general principles of law are indivisible as they are fundamental propositions of law underlying the entire scope of Union law, further support that conclusion.[86] If that argument holds true, in such a case a Member State should, under the general principle that abuse of EU law is prohibited, refuse the benefit of the fundamental freedoms and subject the taxpayer to tax as if he had not made use of his freedoms, even if that Member State would not have adopted appropriate anti-abuse rules or judicial principles. This also seems to be the conclusion reached by Zalasinski[87] and by the authors of the EU report for the 2018 IFA Congress.[88]

This would be an important but also a potentially dangerous development. In the past the CJEU has been very reluctant to uphold abuse of the fundamental freedoms by taxpayers. In the few cases in which the referring court asked whether the taxpayer's conduct constituted such an abuse, the CJEU has answered that question negatively. It subsequently examined whether the prevention of tax avoidance could justify the restriction of the treaty freedoms and whether the national anti-abuse rule was a proportionate measure to strike down the alleged abusive tax practice.[89] Hence, contrary to what it has decided in its recent case law under the VAT-Directive and PSD and IRD, the CJEU has to our knowledge never applied the abuse of EU law-principle as an autonomous exception to the treaty freedoms. In matters of primary EU law, this is a wise policy. It allows the CJEU to consider the effects of the national anti-abuse rule so that the rights of the taxpayer are optimally protected from the point of EU law and exceptions to the Treaty freedoms are construed strictly.[90] If Member States would be forced to deny access to the Treaty freedoms under the general principle that abuse of EU law is prohibited, there is, like we argued above with respect to the Directives, a serious risk that that principle will be misapplied and that taxpayers would wrongfully be denied access to the Treaty freedoms. Such could undermine the construction of the internal market. We even fear that the CJEU would no longer be required to test whether the application of the general principle leads to a discrimination or a restriction as it has done systematically where a domestic anti-abuse rule was at stake. Arnull has warned for such a negative effects of the general principle: '*It is therefore submitted that the prohibition of abuse is too uncertain in its application and potentially damaging to the proper functioning of the Union to be accorded the constitutional status of a general principle of Union law*'.[91]

In the end, as a result of the developments in EU tax law discussed above, today the question is only relevant outside the area of corporate tax (*see* above sub 3.1).

4 When does a Conduit Company Abuse the Exemptions of Withholding Tax under the PSD or IRD?

4.1 Indicators of Abuse in Case of Conduit Companies

As the referring Danish court explicitly asked the CJEU to describe the constituent elements of abuse in the cases at hand and how those element had to be established, the CJEU depicts in significant detail when an interposed company (such as the Luxembourg, Swedish and Cyprus companies interposed between the Danish payor and the third State companies ultimately receiving the dividends or interest) may abuse the PSD and IRD.

The CJEU commences by making some general comments.[92] Starting from the objectives pursued by the PSD and IRD, it says that the setting up of financial arrangements whose sole or essential aim is to benefit from the exemption of withholding tax would not be in accordance with the objectives of the PSD (said to be the facilitation of the grouping of companies through the introduction of tax neutral rules) and the IRD (said to be the elimination of double taxation and achieving single taxation of interest and royalties within the EU with a view to achieving equal tax treatment between domestic and cross-border transactions and reduce

[84] CJEU, 22 Nov. 2017, C-251/16, *Cussens and Others*, § 30.

[85] *See* in particular, CJEU, 12 Sept. 2006, C-196/04, *Cadbury Schweppes*, § 66–67.

[86] Tridimas, *supra* n. 54, at 1.

[87] According to the author: '*The "reinforced" general principle of abuse of rights applies to subjective rights derived from EU legislation. It follows that the principle does not create any new, unwritten norms obliging Member States' authorities to combat abuse or other subjective rights derived from domestic legislation or tax treaties (i.e. rights not derived from EU law)*' (Zalasinski, *supra* n. 67, at 17). As reliance on a fundamental freedom is a subjective right derived from the TFEU, we believe that the author takes the position that Member States have a duty to deny the benefits of the fundamental freedoms in case they are abused for tax purposes.

[88] According to the authors: *'The prohibition of abusive practices is currently described by the Court as a general principle of EU law and, as such, has an inherent and comprehensive character. It applies to harmonized and non-harmonized areas and does not require transposition'* (Garcia Prats et al., *supra* n. 19, at 65).

[89] CJEU, 12 Sept. 2006, C-196/04, *Cadbury Schweppes*, §§ 23–24; CJEU, 21 Nov. 2002, C-436/00, *X&Y AB*, §§ 26, 40 and 60.

[90] De Broe, *supra* n. 4, at 899.

[91] Arnull, *supra* n. 27, at 21.

[92] CJEU, 26 Feb. 2019, PSD-case §§ 78–81, IRD-case §§ 85 and 106–09.

administrative burdens and cash flow problems).[93] The CJEU continues by saying that the general EU law principle that abuse of EU law is prohibited sets a limit to the right of the taxpayer to enjoy the most advantageous tax regime and to engage in jurisdiction shopping. Referring to, inter alia, its holding in *Cadbury Schweppes*, it concludes this part by noting that the taxpayer cannot enjoy a right or advantage arising from EU law where the transaction is purely artificial economically and is designed to circumvent the application of the legislation of a Member State. It then turns to the determination of when an interposed entity abuses the provisions on the exemption of withholding taxes under the PSD or IRD.

Referring to the so-called double test of abuse which it developed in the *Emsland Stärke*-case, the CJEU holds:

> *(…) proof of abusive practice requires, first, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the EU rules, the purpose of those rules has not been achieved and, second, a subjective element consisting in the intention to obtain an advantage from the EU rules by artificially creating the conditions laid down for obtaining it.*

The CJEU adds, referring to earlier case law, that an examination of all facts and circumstances is needed to establish whether the disputed transactions are purely formal or artificial and devoid of any economic and commercial justification and have been set up with the essential aim of benefiting from an improper advantage.[94]

According to the CJEU, a group of companies may be regarded as being an artificial arrangement where it is not set up for reasons that reflect economic reality, its structure is purely one of form and its principal objective or one of its principal objectives – note that again the CJEU is not very rigid in the choice of its terminology as these terms are not used in the PSD or IRD but in Article 15 of the MD[95] – is to obtain a tax advantage running counter to the aim of the applicable tax law. That is so, inter alia, where on account of a conduit entity interposed in the structure of a group between the distributing or paying company and the entity which is the BO of the income, payment of the tax on the dividend or interest is avoided.[96] In other words, according to the CJEU conduit companies are artificial constructions in so far as they allow the income to be passed free of EU withholding tax to a third person which in the eyes of the CJEU is the BO thereof. Of course, that can only be the case if the BO of the income is a person that, for whatever reason, is not able to enjoy the benefits of the Directive (third State resident, disqualifying EU based entity, individual etc.). In our view, there is a tax advantage (that might qualify as tax abuse provided that the double test is met) as soon as the overall withholding tax burden on the interest or dividend payments reduces by interposing the conduit. This could for example be the case when the Member State of the conduit would levy withholding tax on the payments made to the BO that is lower than the withholding tax that the Member State of the distributing or paying company would levy in case of a direct payment to the BO, e.g. the overall withholding tax burden drops from 25% (i.e. 25% withholding tax in the source Member State) to 10% (i.e. 0% withholding tax in the source Member State and 10% in the conduit state) by interposing a conduit company.

The CJEU then sums up number of indicators of when a conduit company is an artificial arrangement. That is so, first, where all or almost all of the dividends or interest received, is very soon after its receipt, passed on by the recipient company to entities which do not fulfil the conditions for enjoying the benefits under the PSD or IRD.[97] Note that this is a double test which concerns the amount of the income that is paid on and the timing of that payment. Second, artificiality can be proven if the taxable profit made by the interposed entity is insignificant because it must pay on all or almost all of the income that it received.[98] This begs the question on when the margin is high enough and when the time lapse is long enough. Here, the CJEU implicitly introduces the notion of risk in the equation, while in another abuse-case it explicitly mentioned the absence of commercial risk as an indication of abuse.[99] Indeed, contrary to a company that receives dividends or interest and uses that income to reinvest or to discharge unrelated liabilities, a company that is compelled to pay on all or most of what it receives (and eventually only if it receives income) does not run financial (or currency) risk and that may be an indication of abuse of the PSD or IRD.[100] Third,

[93] Some authors have therefor argued that it is not evident to refuse the benefits of the IRD to an interposed Luxembourg entity which in the absence of the Directive would be faced with double taxation, cash flow problems and administrative burdens. From that it would follow that the categorical refusal to grant the benefits to an interposed entity (formal recipient) would not be permitted (Boulogne, *supra* n. 45, at 54–55). The author seems to forget that another objective of the IRD is to achieve single taxation of interest within the EU. Such is not the case where interest flows free of withholding tax from Denmark via Luxembourg to third State residents.

[94] CJEU, 26 Feb. 2019, PSD-case §§ 97–98, IRD-case §§ 124–25.

[95] De Broe & Gommers, *supra* n. 41, referring to the CJEU using interchangeably expressions for describing the taxpayer's intention that may have a very different meaning in tax matters such as '*sole purpose*', '*essential aim*', '*principal purpose*' etc. and thereby not paying much attention to the words of the anti-abuse provisions used in the Directives.

[96] CJEU, 26 Feb. 2019, PSD-case § 100, IRD-case § 127.

[97] CJEU, 26 Feb. 2019, PSD-case § 101, IRD-case § 128.

[98] CJEU, 26 Feb. 2019, PSD-case § 103, IRD-case § 130.

[99] CJEU, 13 Mar. 2014, C-155/13, *SICES*, § 39. Compare also to Art. 29, § 182 OECD Comm. and some of the examples quoted there which consider the presence or absence of risk for determining whether an interposed entity would claim inappropriate treaty benefits.

[100] D. Weber, *The New Common Minimum Anti-Abuse Rule in the Parent-Subsidiary Directive: Background, Impact, Applicability, Purpose and Effect*, Intertax 124 (2016).

artificiality of a conduit company is established where the company's sole activity is the receipt of dividends or interest and its transmission to other conduits or the BO. The absence of economic activity must, in light of the special features of that economic activity be inferred from an analysis of all relevant factors, in particular: the management of the company, its balance sheet, the structure of its costs and expenditure actually incurred as well its staff, premises and equipment.[101] What the CJEU suggests is that the lack of economic activity and substance of the conduit company is to be inferred from a series of factual circumstances such as the company's low amount of equity or high amount of intercompany debt, its low amount of management or salary expenses, the fact that its address is situated at that of a company specialized in managing other companies, the fact that the conduit has no staff but uses the services of such a specialized company, including the supply of board members etc. Abuse of the withholding tax exemptions under the PSD and IRD is to be established by the fact that an interposed company frustrates the objectives of those Directives. The grouping together of companies of different Member States with a view to strengthen EU undertakings and to increase their productivity and competitiveness – which are stated objectives of the PSD – supposes that companies carry on genuine economic activities within the EU. It does not extend to brass plate companies and letterbox companies merely passing on profit from a Member State to third countries.[102] On the other hand, as the objectives of the PSD or IRD are not the same as those underlying the TFEU freedom of establishment for which economic substance in the State of secondary establishment is required, the fact that the interposed company carries on a considerable economic activity and has commercial substance does by no means shield it off from a claim that it abuses the IRD if e.g. a back-to-back loan is routed through that company. The same goes a fortiori where a company is interposed on a large scale in such financial conduit arrangements and uses staff, premises and equipment for that activity.[103] Fourth, other indicators of an artificial arrangement may be the various contracts existing between the companies in the relevant transactions, the way in which those transactions are financed, the valuation of the intermediary companies' equity and the conduit companies' inability to have economic use of the dividends or interest received. In that respect such indications may be inferred not only from contractual or legal obligations of the company receiving the income to pass it on to a third party but also from the fact that 'in substance' the company, without being bound by such obligation does not have the right to use and enjoy those sums.[104] Although the CJEU does not explicitly refer to the 2014 OECD Commentary on Article 10 and 12 OECD Model and the interpretation of BO given there, it seems to do so implicitly. It should, however, be noted that the Commentary is more nuanced than the CJEU making clear that the contractual or legal obligations to which it refers are those that are dependent on the receipt of the payment, but not those that are independent from such a receipt and which the recipient may have as debtor under an unrelated financial transaction (*see* below sub 5.1).[105] This again shows that whether the conduit assumes risk may be a useful indicator of abuse. Lastly, the CJEU observes that such indications may be reinforced by the simultaneity or closeness in time of, on the one hand, the entry into force of major new tax legislation, such as the Danish legislation in the main proceedings (*see* above sub 1), which some groups tried to circumvent and, on the other hand, the setting up of complex financial transactions and the grant of intragroup loans.[106] In the authors' view, while the first four indicators are objective circumstances that are capable of establishing that the interposed company frustrates the objectives of the PSD or IRD and of establishing the taxpayer's tax savings intention, the latter indicator merely the demonstrates that the structuring of the transaction is driven by tax avoidance motives.

The CJEU was asked whether it is relevant for determining whether there is an abuse of rights under the PSD or IRD, that the BO of the income passed on by the conduit company is a resident of a third State that has a tax treaty with Denmark that provides for an exemption of withholding tax if the dividends or interest were to be paid directly by the Danish payor to that third State resident who is the BO thereof (*see* below sub 5.4.3 on the question whether this statement introduces an implicit BO requirement to the PSD). We would not hesitate to answer that question affirmatively. The fact that the State of source (Denmark) does not levy withholding tax where the income is paid directly to the BO in a third State is a clear indication that the interposition of the conduit company in an EU Member State is not driven by the intention to avoid tax in Denmark. Accordingly, the second component of the *Emsland Stärke* abuse-test is not met and abuse of the PSD or IRD exemptions of Danish withholding tax is not at stake. The CJEU has a different and confusing meaning though.[107] As a matter

[101] CJEU, 26 Feb. 2019, PSD-case § 104, IRD-case § 131.
[102] De Broe, *supra* n. 4, at 1014–15.
[103] A perfect illustration of this is the Limitation of Benefits-clause ('LOB') included in the OECD Multilateral Instrument which provides for several rules excluding interposed entities from the benefits of a tax treaty, but also provides for a safe harbour rule for companies carrying on *bona fide* commercial operations. As the latter companies could also be used for certain financial conduit arrangements the purpose of which is to benefit from the reduced withholding tax rate in the State of source, the LOB needs to be supplemented by domestic or treaty based anti-conduit rules to prevent those companies from improperly claiming treaty benefits for those arrangements (2017 OECD Commentary on Art. 29, §§ 3, 68 et seq. and 187).
[104] CJEU, 26 Feb. 2019, PSD-case § 105, IRD-case § 132.
[105] *See* e.g. 2014 OECD Commentary on Art. 10, § 12.4.
[106] CJEU, 26 Feb. 2019, PSD-case § 106, IRD-case § 133.
[107] CJEU, 26 Feb. 2019, PSD-case §§ 107–110, IRD-case §§ 134–37.

of principle the CJEU says that the existence of such a tax treaty cannot in itself rule out an abuse of rights where the taxpayer has set up a purely formal or artificial transaction '*with the essential aim of benefitting improperly from the exemption from any taxes*' under PSD or IRD. For the reasons just mentioned we disagree with this view. In paragraph 109 of the PSD-judgment, the CJEU seems to be missing the point:

> *It should be added that whilst taxation must correspond to economic reality, the existence of a double taxation convention is not, as such, capable of establishing that a payment was really made to recipients in third states with which that convention has been concluded. If the company owing the dividends wishes to benefit from the advantages of such convention, it is open to it to pay the dividends directly to the entities that are resident for tax purposes in a State which has concluded a double tax convention with the source State.*

With all due respect but this is non-sensical. A group of companies can only establish that it has no intention to avoid withholding tax in the State of source if it has duly established that the income that arose in the State of source has been paid through the conduit company to the BO in the third State that has concluded the tax treaty with the State of source that offers equivalent benefits as the PSD or IRD. Of course, one cannot demonstrate that a direct payment has been made from the State of source to the third State BO, although that this is the economic reality to which the CJEU refers. It is the existence of the treaty between those two States that establishes the absence of a tax avoidance motive and indirectly the presence of non-tax motives, i.e. sound commercial reasons for setting up the interposed entity in an EU Member State (e.g. a regional HQ holding the EU part of a non-EU multinational group).[108] The CJEU seems to realize that it is on shaky grounds here and concludes this chapter in paragraph 110 as follows:

> *That said, it remains possible, in a situation where the dividends would have been exempt had they been paid directly to the company having its seat in a third State, that the aim of the group's structure is unconnected with any abuse of rights. In such a case a group cannot be reproached for having chosen such a structure rather that direct payment of the dividends to that company.*[109]

A very relevant question is of course how many of the above indicators need to be present before one may conclude that an interposed company abuses the withholding tax exemptions under the PSD or IRD. The only thing which the CJEU elucidates is that more than one of such indicators needs to be present and that those indicators need to be objective and consistent:

> *The presence of a certain number of indications may demonstrate that there is an abuse of rights, in so far as those indications are objective and consistent. Such indications can include, in particular, the existence of conduit companies which are without economic justification and the purely formal nature of the structure of the group of companies, the financial arrangements and the loans. The fact that the Member State where the interest arises has concluded a convention with the third State in which the company that is the beneficial owner of the interest is resident has no bearing on any finding of an abuse of rights'.*[110]

For assessing these indicators in concrete cases, the 2017 OECD Commentary on Article 29 (Principal Purposes Test) may be an interesting source of inspiration. It shows how difficult, for purposes of determining whether treaty benefits are (in)appropriately claimed, the weighing may be of the different objective factors of the case and of taxpayer's business motives and tax savings intentions where intra-group holding, financing or IP companies and collective investment vehicles (CIV) and securitization vehicles are set up.[111]

Authors seem to be in disagreement about the role which the CJEU has attached to the subjective element of the abuse-test, i.e. the taxpayer's intention to claim tax benefits under the Directives. According to Boulogne, the relative importance of that subjective element has increased after the CJEU's judgments in the PSD and IRD-cases.[112] On the other hand, Zalasinski argues the opposite.[113] We believe, however, that these judgments do not establish a change in the CJEU's approach. The CJEU starts its analysis of the constituent elements of abuse by referring to the two prong-test it developed in its *Emsland Stärke*-judgment to establish when an economic operator abuses his rights under EU (secondary) law. The CJEU notes that one has to establish on the basis of the circumstances of the particular case whether the objective component (frustration of the objectives of the PSD or IRD) as well as the subjective component (the taxpayer's tax saving motive) of that test are met. If that analysis leads to the conclusion that the transactions are purely formal or artificial, devoid of any economic and commercial justification and executed with the essential aim (also depicted by the CJEU as principal objective or

[108] Compare to examples G, H and K in 2017 OECD Commentary on Art. 29, § 182.

[109] Similar holding in CJEU, 26 Feb. 2019, PSD-case, § 110.

[110] CJEU, 26 Feb. 2019, IRD-case § 139. Remarkably the conclusion in the judgment in the PSD case in § 114 is the same but the last sentence is missing. Does the CJEU realizes that the sentence does not make sense?

[111] For a critical assessment of the 2017 OECD Commentary and its examples conceived to clarify the functioning of the Principal Purposes Test under Art. 29 OECD Model, *see* S. van Weeghel, *A Deconstruction of the Principal Purposes Test*, World Tax J. (3–45) Feb. 2019.

[112] Boulogne, *supra* n. 45, at 55.

[113] Zalasinski, *supra* n. 67, at 11–15, in particular at 15: '*Indeed, the rock-solid approach according to which the taxpayer may have tax motives for exercising the fundamental freedoms as long as he carries on genuine activities seems to be seriously eroded, if not abandoned. This outcome seems surprising, since as noted above, the ECJ disallowed the motive-test in cross-border situations only and applied fairly lenient criteria for genuine establishment until very recently*'.

one of its principal objectives, *see* above sub 4.1) of benefiting from the withholding tax exemptions under the PSD or IRD, abuse of EU law is to be upheld. The first four indicators of abuse establish both the objective and subjective component of the *Emsland Stärke*-test, while the fifth one only concerns the subjective component.

4.2 Burden of Proof

With respect to the burden of proof, a distinction needs to be made between the burden of proving that the income recipient is entitled to the withholding tax exemptions in the Member State of source and the burden of proving an abuse of rights. So the CJEU holds that under the PSD the taxpayer has the duty to establish that he meets the conditions for enjoying the exemption of withholding tax in the State of source of the dividends and that it follows from Article 1 (11), (12) and (13b) of the IRD that the company that has received the interest has the duty to prove that it is the BO thereof.[114] This is logic as it is up to the taxpayer who claims an exemption to establish that he meets the formal conditions for that exemption. However, when the tax authorities of the source State seek, on grounds relating to the existence of an abusive practice, to refuse the exemption of withholding tax under either of these Directives, they must establish the existence of the elements constituting such a practice while taking account of all relevant factors, in particular the fact that the company receiving the dividends or interest is not the BO thereof. This is in line with earlier CJEU case law on tax abuse.[115] On the other hand, according to the CJEU the tax authorities should not identify the true BO. Such may be a too complex and amount to an impossible proof for the tax authorities of the State of source given the complexity of the financial transactions and the fact that the BO's are established outside the EU. Even if the potential BO's are known, it is not necessarily established which of them are or will be the BO's and what amount they have received. Also, allocation of the dividends or interest may be decided after the tax authorities' finding that the conduit company abuses the Directives.[116] For all these reasons, the CJEU concludes that it suffices that the tax authorities of the State of source establish that the entity formally receiving the income has been interposed abusively.[117]

The division of the burden of proof as proposed by the CJEU seems to be a reasonable one. However, the fact that the tax authorities are not required to establish the BO's when abuse is proven precludes taxation as if no abuse has occurred, which is in the authors' view required under the CJEU's judgment in *Halifax* (*see* below sub 6.2.2).

[114] CJEU, 26 Feb. 2019, PSD-case §§ 115–16, IRD-case §§ 140–41.
[115] CJEU, 21 Jan. 2010, *SGI*, C-311/08, §§ 73–75.
[116] Although the passing of a certain time span between the receipt of the income by the conduit and the payment to the BO may be an indication of the absence of abuse (*see* above sub 4.1).
[117] CJEU, 26 Feb. 2019, PSD-case §§ 117–20, IRD-case §§ 142–45.

5 Beneficial ownership (BO)

5.1 The OECD's BO Concept

A second series of questions referred to the CJEU relates to the interpretation of the BO concept. It is the first time that the CJEU is called upon to shed its light on the boundaries of BO, which is arguably the most discussed term in international tax law. Before we examine the CJEU's judgment, we will first briefly touch upon the origin and use of the OECD's BO concept and its relevance for the IRD and PSD.

The BO concept in the OECD Model is used to restrict a source State's right to tax[118] as well as to assure an appropriate taxation of business profits[119] and of non-arm's length interest and royalty payments in the source State.[120] It was introduced in the 1977 OECD Model to prevent that treaty benefits would be granted in a situation that was not intended by the treaty. The historical OECD materials elucidate that the BO concept was preferred over a subject-to-tax clause, according to which treaty benefits are dependent on the question whether a payment is subject to tax in the residence State.[121] This would suggest that the BO concept and subject-to-tax provision both seem to ensure that only persons that are faced with (possible) double taxation can claim treaty benefits (i.e. reduced taxation in the State of source). The historical OECD materials furthermore show that the BO concept intends to exclude agents and nominees from treaty benefits. The reason therefore is that these intermediaries are usually not themselves subject to tax on the income received for the benefit of their principal.[122]

It is remarkable that the historical OECD materials do not contain a clear definition of the term BO. It appears that the principal aim was to ensure that agents and nominees do not qualify as BO. Hence, it is not surprising that the concept was not defined in the 1977 OECD Model and that the 1977 OECD Commentary only provides for an additional clarification stating that '*an intermediary such as an agent or nominee*' could not benefit from the reduced source taxation unless the BO is resident in the other contracting State, i.e. the residence State.[123]

[118] Art. 10 (2), 11 (2) and 12 (1) OECD Model.
[119] Art. 10 (4), 11 (4) and 12 (3) OECD Model.
[120] Art. 11 (6) and 12 (4) OECD Model.
[121] J. Schwarz, *Schwarz on Tax Treaties,* no. 25–300 (5th Ed., Alphen aan den Rijn: Kluwer Law International 2018).
[122] For an extensive overview we refer to R. Vann, *Beneficial Ownership: What Does History (and Maybe Policy) Tell Us* in *Beneficial Ownership: Recent Trends* 281–307 (M. Lang, P. Pistone et al. eds, IBFD 2013); A. Meindl-Ringler, *Beneficial Ownership in International Tax Law*, Series on International Taxation, Volume 58, 14–32 (Kluwer Law International 2016).
[123] Art. 10, § 12, 11, § 8 and 12, § 4 OECD Comm. 1977.

It took the OECD until 2003 to substantially amend the OECD Commentary as regards the BO concept.[124] First, the 2003 OECD Commentary clarifies that the BO concept should not be used in a narrow technical sense, but that it should be understood in its context and in the light of the object and purpose of a double tax treaty. This object and purpose includes the avoidance of double taxation but also the prevention of fiscal evasion and avoidance.[125] The 2003 OECD Commentary also clarifies that where the recipient simply acts as conduit for another person who in fact receives the benefit of the income, the recipient does not qualify as BO. A conduit company can in principle not qualify as BO if it has as a practical matter very narrow powers which render it, in relation to the income received, a mere fiduciary or administrator acting on account of the interested parties, notwithstanding the fact that it is the formal owner of the income.[126] Finally, the 2003 OECD Commentary makes clear that the limitation of source State taxation remains available if an intermediary is interposed but the BO is resident in the other contracting State, i.e. the residence state.[127]

In 2014 numerous clarifications were again added to the OECD Commentary as regards the BO concept. The 2014 OECD Commentary first clarifies that the BO concept does not refer to any technical meaning the concept could have under domestic law of a specific country.[128] This implies that BO has an international tax meaning. It has been further clarified that agents, nominees and conduit companies acting as a fiduciary or administrator, do not qualify as BO if their right to use and enjoy the income is constrained by a contractual or legal obligation to pass on the payment received to another person. Such obligation does not include legal or practical obligations that are not dependent on the receipt of the payment. The existence of an obligation to pass on the payment received typically derives from relevant legal documents but it may also exist on the basis of facts and circumstances showing that 'in substance' the recipient of the income does not have the unconstrained right to use and enjoy that income.[129] Furthermore, the Commentary makes it clear that the BO-concept is concerned with the BO of the income and not with the owner of the underlying asset from which the income originates.[130]

The 2014 OECD Commentary further clarifies that treaty benefits can be denied to the BO based on other anti-avoidance rules.[131] The BO concept targets a specific form of tax abuse, i.e. the interposition of a recipient who is obliged to pass on the income received. Hence, BO does not restrict the application of other anti-abuse provisions addressing treaty shopping by conduit companies. And finally, the 2014 OECD Commentary confirms once again that reduced taxation in the source State remains available in case an intermediary is interposed between the BO of an income and the payer of that income, if the BO is resident in a contracting state irrespective of the State of residence of the intermediary.[132]

A final series of changes to the BO concept was made in the 2017 version of the OECD Commentary. These changes are, however, limited and are mainly intended to clarify that the qualification as BO does not prevent the application of anti-abuse rules, in particular the new Article 29 OECD Model which includes a Limitation on Benefits (LOB)-clause and PPT.[133]

It is clear from the foregoing that the clarity of the OECD's BO concept increased over the years. During the past decades, the meaning of the term BO has been the subject of numerous discussions between scholars and judges in tax courts. Although the BO concept is generally given an autonomous international tax meaning, the opinions differ as regards its exact contours. On the one hand, the BO concept has been given a narrow and legal interpretation according to which the person that is legally entitled to enjoy the income is considered as BO.[134] On the other hand, the BO concept has also been given, often pursuant to a 'substance over form'-examination, a broad and economic interpretation which focusses on the economics of the structure.[135] As from the 2014 and 2017 changes to the OECD Commentary, it leaves no doubt that the BO concept focusses on an obligation for the recipient of the income to pass on the income received to another person. It is only when the recipient of income has a binding obligation to pay that particular income to another person, that such recipient cannot qualify as BO.[136] Furthermore, because the BO requirement deals with a specific type of tax abuse (i.e. the interposition of a recipient who is obliged to pass on the income received) and does not restrict the application of other anti-abuse provision against treaty shopping, it is clear that the BO requirement is not a broad anti-abuse provision.

[124] Please note for completeness sake that the BO concept in Art. 10 (2) and 11 (2) OECD Model was slightly amended in 1995 and that the BO concept in Art. 12 (1) was slightly amended in 1997.
[125] Art. 10, § 12, 11, § 8 and 12, § 4 OECD Comm. 2003.
[126] Art. 10, § 12.1, 11, § 8.1 and 12, § 4.1 OECD Comm. 2003.
[127] Art. 10, § 12.2, 11, § 8.2 and 12, § 4.2 OECD Comm. 2003.
[128] Art. 10, § 12.1, 11, § 9.1 and 12, § 4 OECD Comm. 2014.
[129] Art. 10, § 12.4, 11, § 10.2 and 12, § 4.3 OECD Comm. 2014.
[130] *Ibid.*
[131] Art. 10, § 12.5, 11, § 10.3 and 12, § 4.4 OECD Comm. 2014.
[132] Art. 10, § 12.7, 11, § 11 and 12, § 4.6 OECD Comm. 2014.
[133] E.g. Art. 10, § 12.5, 11, § 10.3 and 12, § 4.4 OECD Comm. 2017.
[134] E.g. CA: Tax Court of Canada, 24 Feb. 2012, *Velcro Canada Inc. v. The Queen*, 2012 TCC 57, IBFD research portal.
[135] E.g. CH: Tribunal Fédéral, 5 May 2015, *X. Sàrl v. Administration Fédérale des Contributions* AFC, 2C 364/2012, IBFD research portal.
[136] P. Baker, *The Meaning of 'Beneficial Ownership' as Applied to Dividends Under the OECD Model Tax Convention*, in *Taxation of Intercompany Dividends Under Tax Treaties and EU Law* 93 (G . Maisto ed., IBFD 2012).

5.2 The EU's Equivalent

In EU tax law the concept BO was introduced in 2003. It is included in the IRD and in the Savings Directive ('*SD*').[137] The term was not included in the original version of the PSD which dates from 1990, nor was it introduced through later amendments.

5.2.1 *Interest and Royalties Directive*

In the wake of the adoption of the PSD in 1990, the European Commission submitted a proposal to abolish withholding taxes on interest and royalty payments between parent companies and subsidiaries located in different EU Member States.[138] The BO concept did not appear in this proposal, which was eventually withdrawn in 1994.[139] A few years later, in 1998, the European Commission submitted an adjusted proposal in which the BO-concept appeared for the first time.[140] According to this proposal, the withholding tax exemption on interest and royalty payments is subject to various conditions, including the fact that the recipient of such payment qualifies as the BO (Article 1 of the Proposal). A BO of an interest or royalty payment is defined as '*a company of a Member State or a permanent establishment which holds those payments for its own benefit and not as an agent, trustee or nominee for some other person*' (Article 3 (1) (c) of the Proposal).

The explanatory memorandum of this 1998 proposal clarifies that the term BO '*is intended to secure that the [withholding tax*, authors' addition*] exemption applies when an intermediary, such as an agent or nominee or trustee, is interposed between the beneficiary and the payer, only if the true owner of the interest or royalty payment meets the requirements of the Directive*'. In other words, the BO requirement should ensure that the withholding tax exemption is not wrongfully obtained by interposing an intermediary. Furthermore, it should be noted that no reference is made to the OECD's BO concept. This is remarkable because such reference is made as regards the definition of the terms '*interest*' and '*royalties*'. For those two terms the explanatory memorandum explicitly states that these are based on the definitions used in Article 11 resp. Article 12 of the 1996 OECD Model.[141]

The 1998 proposal eventually resulted in the adoption of the IRD in 2003. Although the underlying aim remained the same, the final version of the IRD deviates in certain ways from the 1998 proposal. As regards the BO definition, the IRD states that a company of a Member State is treated as the BO of interest or royalty payments '*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*' (Article 1 (4) of the IRD). Contrary to the 1998 proposal, it follows from the expression '*such as*' that the enumeration of the recipients that do not qualify as BO is not exhaustive.

A permanent establishment on the other hand, is treated as the BO of interest or royalty payments:

> *(i) if the debt-claim, right or use of information in respect of which interest or royalty payments arise is effectively connected with that permanent establishment, and (ii) if the interest or royalty payments represent income in respect of which that permanent establishment is subject in the Member State in which it is situated to one of the taxes mentioned in […]* (Article 1 (5) of the IRD).

This specific BO requirement for PE's can be explained by the fact that PE's are not separate legal entities and can therefore not benefit from a payment.[142] That is why a connection should exist between the payment and the recipient, i.e. the PE. Moreover, because companies should comply with a subject-to-tax requirement to benefit from the IRD (Article 3 (a) (iii) of the IRD), a subject-to-tax clause has been included in the BO requirement for PE's. Finally, if a PE is treated as the BO of a payment, no other part of the company can qualify as BO (Article 1 (6) of the IRD).

The recitals to the IRD do not clarify why the BO-concept is included in the IRD. Moreover, the recitals do not contain any reference to the OECD's BO concept, nor is any reference to the 1996 OECD Model maintained as regards the interpretation of the terms '*interest*' and '*royalties*'.

From the foregoing, it follows that there are quite some differences between the 1998 proposal and the IRD. In addition to some linguistic differences, the main difference relates to the non-exhaustive enumeration of recipients that do not qualify as BO and the inclusion of a specific BO requirement for PE's. Because the aim of the IRD did not change compared to the 1998 proposal, we believe that the explanatory memorandum is still relevant for the interpretation of the IRD's BO concept as applicable to companies (Article 1 (4) of the IRD).

Although not explicitly mentioned in the 1998 proposal nor in the recitals to the IRD, the European

[137] Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income in the form of interest payments.

[138] Proposal for a Council Directive on a common system of taxation applicable to interest and royalty payments made between parent companies and subsidiaries in different Member States, COM(90) 571 final of 6 Dec. 1990.

[139] EU Commission press release IP/94/1023 of 8 Nov. 1994.

[140] Proposal for a Council Directive on a common system of taxation applicable to interest and royalty payments made between parent companies of different Member States, COM (1998) 67 final of 4 Mar. 1998.

[141] In 1992 the OECD decided to publish the OECD Model and the Commentary thereto in a loose-leaf format that was subject to an ongoing revision process resulting in periodic updates (Introduction § 8, OECD Comm. 2017). We assume therefore that the reference to the 1996 OECD Model and 1996 OECD Commentary is in fact a reference to the 1992 OECD Model and 1992 OECD Commentary including the updates made in 1994 and 1995.

[142] Meindl-Ringler, *supra* n. 122, at 301.

Commission has without any doubt found inspiration with the OECD's BO concept. There is no other reasonable explanation for the fact that the well-known BO concept relevant for the limitation of source taxation in accordance with double tax treaties suddenly is introduced in the IRD.

However, we believe that the IRD's BO concept is to be interpreted autonomously, i.e. the IRD's BO concept has an own meaning.[143] The reason therefore is threefold. First and foremost, the IRD contains a proper definition of BO. For example, in the IRD's BO concept trustees are explicitly excluded whilst trustees can qualify as BO in certain circumstances following the OECD Commentary.[144] Second, the 1998 proposal, nor the IRD refer to the OECD's BO concept. Hence, the concept cannot be interpreted solely on the basis of the OECD's BO concept. This is different for the interpretation of the terms interest and royalties, for which the 1998 proposal made an explicit reference to the 1996 OECD Model (that is, however, not retained in the IRD's recitals). Finally, international tax law and EU tax law are different and have their own interpretation methods.[145] The interpretation of double tax treaties is in principle governed by the general rules to interpret international law which constitute customary international law and are codified in the Vienna Convention on the Law of Treaties, and the specific interpretive rules in the double tax treaties, such as Article 3 (2) of the OECD Model.[146] EU (tax) law, on the other hand, has its own interpretation methods, in which the teleological interpretation method plays an important role.[147]

However, when it comes to determining the exact meaning of the BO concept in the IRD, the situation is more difficult. First, as explained below, the definition included in the IRD is ambiguous and not that clear as to when a recipient qualifies as BO. Furthermore, a few years after the adoption of the IRD, the European Commission published a report according to which the BO concept is specifically designed to tackle artificial conduit arrangements. This position was supported by a reference to the case law of the CJEU as regards the fundamental freedoms and tax abuse whilst such case law was not yet existing when the IRD was adopted.[148,149] The Commission furthermore states that it can be doubted whether a company that qualifies as the BO could be considered an artificial conduit pursuant to the application of the 'anti-abuse reservation of competence' laid down in Article 5 of the IRD (see above sub 1). The Commission thus sees a certain connection between the BO concept and the CJEU's case law on tax abuse. It implicitly seems to argue that the BO requirement is a specific form of abuse in the sense of the relevant anti-abuse case law of the CJEU.

Various scholars are of the opinion that there are good arguments to defend that the BO concept is to be interpreted economically and not from a legal point of view.[150] We believe, however, that the exact meaning of the BO-concept cannot be derived from the IRD. On the one hand there are arguments in favour of an economic interpretation, such as the condition that a BO receives the payments '*for its own benefit*', which appears to indicate that there must be an economic benefit for the recipient. This would imply that as soon as a recipient of a payment realizes a certain benefit (e.g. an arm's length spread on an intercompany loan in a back to back situation), this is sufficient to qualify him as BO.[151] On the other hand, we believe that there are also arguments that support a more narrow and legal interpretation, such as the fact that the BO concept stresses the legal qualification of the recipient of the interest payment, i.e. '*not as an intermediary, such as an agent, trustee or authorised signatory*'.[152] This suggests that a person receiving income in its own name and for its own account is the BO of that income. Moreover, the CJEU clarified that the minimum holding period that is a condition to apply the PSD, is to be interpreted strictly because it constitutes a derogation from the principle of withholding tax exemption.[153] It can therefore be argued that the BO requirement, which also serves as a requisite to benefit from the withholding tax exemption in the IRD, is also to be interpreted strictly.

143 In the same sense: D. Weber, *The Proposed EC Interest and Royalty Directive* 22 (ECTR 2000); L. Hinnekens, *European Commission Introduces Beneficial Ownership in Latest Tax Directives Proposals Adding to the Confusing With Regards to Its Meaning* ECTR 44 (2000); S. M. Fernandes, R. Bernales, S. Goeydeniz, B. Michel, O. Popa & E. Santoro, *A Comprehensive Analysis of Proposals to Amend the Interest and Royalty Directive – Part 1*, ET 402 (2011); J. M. Terra & P. J. Wattel, *European Tax Law* 763 (Sixth ed., Kluwer Law International 2012); J. L. Rodriguez & G. Kofler, *Beneficial Ownership and EU Law,* in *Beneficial Ownership: Recent Trends* 237 (M. Lang, P. Pistone et al. eds, IBFD 2013); Meindl-Ringler, *supra* n. 122, at 300.

144 Art. 10, § 12.1, footnote 1 OECD Comm.

145 Hinnekens, *supra* n. 143, at 44.

146 In the case C-648/15 the CJEU was called upon to interpret the double tax treaty concluded between Austria and Germany. The Court, however, ruled that the specific interpretation rule included in Art. 3 (2) of this double tax treaty could not be applied because this rule cannot be regarded as intended to arbitrate between divergences of interpretation between the two contracting states (CJEU, 12 Sept. 2017, *Austria v. Germany*, C-648/15, § 36).

147 K. Lenaerts & J. A. Gutiérrez-Fons, *To Say What the Law of the EU Is: Methods of Interpretation and the European Court of Justice*, 9 AEL 24 (2013).

148 Report from the Commission to the Council in accordance with Art. 8 of Council Directive 2003/49/EC on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, Com(2009) 179 final, 8.

149 The first CJEU case in the field of direct taxation that relates to tax abuse was delivered three years after the adoption of the IRD, i.e. CJEU, 12 Sept. 2006, *Cadbury Schweppes*, C-196/04.

150 Weber, *supra* n. 143, at 23; Hinnekens, *supra* n. 143, at 44; M. Distaso & R. Russo, *The EC Interest and Royalties Directive – A Comment*, ET 148 (2004); Fernandes, Bernales, Goeydeniz, Michel, Popa & Santoro, *supra* n. 143, at 404.

151 Distaso & Russo, *supra* n. 150, at 149.

152 De Broe, *supra* n. 4, at 675.

153 CJEU 17 Oct. 1996, C-283/94, *Denkavit*, § 27.

Because of the ambiguous meaning of BO, practitioners looked at the CJEU to resolve the existing ambiguity and give a practical interpretation to the IRD's BO concept. It is has now finally tried to do so in the IRD-case (*see* below sub 5.3.1).

5.2.2 Savings Directive

For completeness sake, it should be noted that the BO concept was also included in the SD, that has been repealed in the meantime.[154] When the Directive on freedom of capital movements was adopted in 1989, a proposal to levy a uniform withholding tax on interest paid within the Union was submitted.[155] This proposal was however never adopted. In 1998 a new attempt was undertaken to introduce a directive to ensure taxation of income from savings. In this new proposal the BO concept was introduced.[156] This new proposal was also unsuccessful because of a lack of consensus amongst the Member States. A third proposal of 2001 appeared to be successful.[157] This proposal was adopted in 2003 together with the IRD (and the Code of Conduct on Company Taxation) and resulted in the SD.

The purpose of the SD was to ensure effective taxation of interest income from savings made in one Member State to an individual who is the BO of that income and who is resident for tax purposes in another Member State in accordance with the legislation of that Member State (Article 1 (1) of the SD). A BO was defined as:

> *any individual who receives an interest payment or any individual for whom an interest payment is secured, unless he provides evidence that it was not received or secured for his own benefit, that is to say that (i) he acts as a paying agent […], (ii) he acts on behalf of a legal person […], (iii) he acts on behalf of another individual who is the beneficial owner […]* (Article 2 (1) of the SD).

Furthermore, if the paying agent has information suggesting that the individual receiving an interest payment or for whom an interest payment is secured may not be the BO, and that this individual is not representing a legal person, the paying agent should take reasonable steps to identify the BO. If the paying agents fails to identify the BO, the individual receiving the interest is deemed the BO, unless the individual demonstrates that he represents a legal person or identifies the BO (Article 2 (2) of the SD).

Like the IRD, the SD also used the BO concept. Because both directives were adopted at the same point in time, one could reasonably expect that the BO concept in these directives refers to the same notion. However, the definition of BO used in both directives is not identical, very likely because the concept serves a different purpose in each directive.[158] In the IRD, the BO concept serves as a condition to ensure that the true owner of the interest or royalty can claim the withholding tax exemption, whilst in the SD the concept is used to ensure that the income from savings is taxed at least once. This difference explains why the SD, contrary to the IRD, contains a rebuttable presumption that an individual receiving interest payments is in some circumstances deemed the BO. Because of the different aim and underlying mechanism, we believe that each concept requires an autonomous definition.

5.3 The Judgments of 26 February 2019

5.3.1 IRD-Case

The CJEU commences its analysis by stating that the IRD's BO concept cannot refer to concepts of national law that vary in scope.[159] Next, it recalls (1) the aim of the IRD (i.e. the elimination of double taxation of interest and royalty payments between associated companies in different Member States and the fact that such payments should be subject to taxation in a single Member State[160]), (2) the scope of the IRD (i.e. application between companies and permanent establishments in two different Member States[161]) and (3) its previous case law according to which only the actual BO can receive interest which constitutes income from debt-claims of every kind in the meaning of the IRD.[162]

From these statements, the CJEU draws the conclusion that the IRD's BO concept defined in Article 1 (4) of the IRD refers to the entity which actually benefits from the interest that is paid to it. According to the CJEU the BO definition therefore refers to economic reality.[163] Moreover, the CJEU finds support for this conclusion in some translations of the BO concept in different language versions of the IRD according to which the term BO does not concern '*the formally identified recipient but rather the entity which benefits economically from the*

[154] Council Directive (EU) 2015/2060 of 10 Nov. 2015 repealing Directive 2003/48/EC on taxation of savings income in the form of interest payments.

[155] Proposal for a Council Directive on a common system of withholding tax on interest income, COM (89) 60 final of 6 Feb. 1989.

[156] Proposal for a Council Directive to ensure a minimum of effective taxation of savings income in the form of interest payments within the Community, COM (1998) 295 final of 20 May 1998.

[157] Proposal for a Council Directive to ensure effective taxation of savings income in the form of interest payments within the Community, COM (2001) 400 final of 19 July 2001.

[158] In the 1998 proposals of the IRD and the SD the BO concept is introduced. In both proposals the definition of BO was already different. One scholar seems to state implicitly that both definitions refer to an [single] autonomous Community concept, which implies that the meaning of both concepts is the same (Hinnekens, *supra* n. 143, at 43).

[159] CJEU, 26 Feb. 2019, IRD-case § 84.

[160] CJEU, 26 Feb. 2019, IRD-case § 85.

[161] CJEU, 26 Feb. 2019, IRD-case § 86.

[162] CJEU, 26 Feb. 2019, IRD-case § 87 with reference to CJEU, 21 July 2011, *Scheuten Solar Technology*, C-397/09, § 27.

[163] CJEU, 26 Feb. 2019, IRD-case § 88.

interest received and accordingly has the power to freely determine the use to which it is put'.[164]

In the first part of its analysis, the CJEU implicitly states that the IRD's BO concept has an autonomous EU meaning. With reference to, amongst others, the aim of the IRD the CJEU rules that the BO concept should be interpreted economically and not formally.

The CJEU continues its analysis and notes that it is apparent from the 1998 proposal (*see* above sub 5.2.1) that the IRD draws upon Article 11 of the 1996 OECD Model and pursues the same objective, i.e. avoiding international double taxation. The CJEU therefore concludes that, the BO concept which appears in double tax treaties based on that model and the successive amendments of that model and the commentaries, 'are relevant' when interpreting the IRD's BO concept.[165] According to the CJEU, it is clear from the development of the OECD Model and OECD Commentary that the BO concept excludes conduit companies and should not be understood in a narrow technical sense.[166] This would also appear from BO concept included in the Danish-Luxembourg Double Tax Treaty and the Nordic Double Tax Treaty.[167]

In the second part of its analysis the CJEU nuances the autonomous meaning of the IRD's BO concept and clarifies that the OECD's BO concept is relevant when interpreting the IRD's BO concept. The CJEU, however, does not provide any guidance as to how the OECD's concept is relevant.

Finally, the CJEU concludes its analysis by stating that if a company that receives an interest payment in a Member State is not the BO, the withholding tax exemption provided by the IRD can still be applicable if the recipient transfers the amount of the interest payment to the BO who is also established in the EU and satisfies all conditions of the IRD.[168] Although the CJEU makes no reference to it, it likely found inspiration for this conclusion in the OECD Commentary that also allows the BO to claim treaty benefits when it receives the income from the intermediary (that does not qualify as BO) provided that all conditions thereto are fulfilled (*see* above sub 5.1).[169]

5.3.2 PSD-Case

In the PSD-case, the CJEU's answer to the questions in relation to BO is straightforward. Taking into account the general principle of EU law prohibiting the abuse of rights and the obligation for Member States to refuse to grant the benefits provided for by EU law in case there is an abusive practice (*see* above sub 3.3), the CJEU finds that there is no need to answer the question whether the BO concept as included in a double tax treaty could be applied as an agreement-based anti-abuse provision.[170] Hence, it is also deems it unnecessary to answer the other questions regarding the BO concept.[171]

However, when addressing the questions in relation to the constituent elements of abuse (*see* above sub 4.1), the CJEU suddenly states that the benefits of the PSD are refused if the BO of the dividends is resident in a third state (irrespective whether there is any fraud or abuse of rights).[172] Albeit the PSD does not contain a BO requirement, the CJEU suddenly seems to implicitly make the PSD's benefits subject to a BO requirement. This is discussed below sub 5.4.3.

5.4 Some Conclusions and Observations on the Judgments of 26 February 2019

5.4.1 The IRD's BO Concept

From the statement that the IRD's BO concept cannot refer to concepts of national law, one could reasonably conclude that the CJEU supports an autonomous interpretation of the IRD's BO concept.[173] It would have been preferable, however, that the CJEU explicitly confirmed this, like the opining AG Kokott did.[174]

Next the CJEU concludes that the IRD's BO concept is to be interpreted economically. It does so after a teleological and a textual interpretation of the IRD. The reasoning of the CJEU is in our view not convincing as one cannot reasonably conclude on the basis of the aim, the scope and some language versions of the IRD that an economic interpretation prevails over a formal interpretation of the BO concept (*see* above sub 5.2.1).

Although the reasoning of the CJEU is not convincing, the outcome that the IRD's BO concept is to be interpreted economically does not come as a surprise in light of the expression '*receives those payments for its own benefit*' used in the definition (*see* above sub 5.2.1). However, it should be noted that AG Kokott opined that the BO within the meaning of the IRD is the person entitled under civil law to demand the payment of the interest.[175] According to the AG, a BO collects a payment in his own name and for his own account, which is not the case for an agent or authorized signatory (as they do not act in their own name) or a trustee (as it does not act for his own account).[176] The AG thus favoured a more legal interpretation of the BO concept, which, as

[164] CJEU, 26 Feb. 2019, IRD-case § 89.
[165] CJEU, 26 Feb. 2019, IRD-case § 90.
[166] CJEU, 26 Feb. 2019, IRD-case § 92.
[167] CJEU, 26 Feb. 2019, IRD-case § 93.
[168] CJEU, 26 Feb. 2019, IRD-case § 94.
[169] Art. 11, § 11 OECD Comm.

[170] CJEU, 26 Feb. 2019, PSD- case § 93.
[171] CJEU, 26 Feb. 2019, PSD- case § 94.
[172] CJEU, 26 Feb. 2019, PSD- case § 111.
[173] Contra: A. Ottosen & S. Andersen, *Preliminary Judgements in the EU Beneficial Ownership Cases*, D&FI 3 (2019). These authors argue that the IRD's BO concept should be understood in accordance with the meaning given under domestic law of the Member States because the CJEU refers to some language versions.
[174] Opinion AG Kokott, 1 Mar. 2018, *N Luxembourg 1*, C-115/16, § 55.
[175] Opinion AG Kokott, 1 Mar. 2018, *N Luxembourg 1*, C-115/16, § 37.
[176] Opinion AG Kokott, 1 Mar. 2018, *N Luxembourg 1*, C-115/16,§ 38.

previously explained, can also be supported (*see* above sub 5.2.1).

Although the CJEU ruled in favour of a more economic interpretation, this does not imply that the content of the BO concept has now become crystal clear. The definition of the IRD's BO concept still remains vague and triggers numerous questions. It is still not clear when a recipient is deemed to benefit '*economically*' from an interest payment, although the clarification in paragraphs 89 of the judgment that the BO should have '*the power to freely determine the use*' to which the income received is put, is helpful and allows to deny BO-status to the most blatant forms of conduit structures. However, this clarification does not resolve all interpretation issues. Imagine that a company receives an interest payment and uses this immediately to reimburse a loan contracted with a financial institution or to pay its suppliers, employees or even its tax liabilities etc. Although the company pays the income received immediately to another person and has in essence no discretion to freely determine what it will do with the interest received, we believe that it still '*economically*' benefits from the interest payment and thus qualifies as the BO. If the expression '*receives those payments for its own benefit*' in the definition of BO in Article 1 (4) of the IRD will be tested by asking whether the recipient of the interest will pay it on to a third party (eventually shortly after receipt), then almost no such recipient will qualify as BO of the interest. This will only be different if we exclude from that expression recipients of interest that are not free to decide to whom they will have to pay it because they have the contractual or legal obligation to pay that specific interest to another person. That brings us to the interpretation proposed by the 2014 OECD Commentary which is discussed hereafter.

5.4.2 *Relevance of the OECD's BO Concept*

In the second part of its BO-analysis, the CJEU nuances the autonomous interpretation of the IRD's BO concept because it finds that the OECD's BO concept in double tax treaties based upon the 1996 OECD Model and the successive amendments of the OECD Model and the OECD Commentary thereto '*are relevant*' when interpreting the IRD's BO concept.[177] Here again, the CJEU deviates from the opining AG, according to whom the IRD's BO concept is to be interpreted autonomously and independently from the OECD's BO concept.[178] The CJEU furthermore clarifies that the BO concept excludes conduit companies and should not be understood in a narrow technical sense with explicit reference to the OECD Commentaries of 1977 and 2003.[179] This seems to suggest that the CJEU believes that the 2014 and 2017 OECD Model and Commentary thereto are not relevant. We do not share this conclusion of the CJEU for various reasons.

The CJEU reaches the above conclusion based on a historical interpretation with reference to the 1998 proposal that served as basis for the IRD (*see* above sub 5.2.1). This is remarkable because the 1998 proposal only refers to the 1996 OECD Model for the definition of the terms '*interest*' and '*royalties*' and for the exclusion from the IRD's benefits of non-arm's length payments. The 1998 proposal makes no reference to the 1996 OECD Model for the interpretation of the BO concept or the interpretation of the IRD in general, nor does the IRD itself or its preamble include such reference. Hence, in our view it cannot be concluded based on a historical interpretation that the OECD's BO concept is relevant when interpreting the IRD's equivalent. If the Commission would have wanted to interpret the IRD's BO concept in accordance with the 1996 OECD Model, it would arguably also have included an explicit reference in the IRD or its preamble.

On the other hand, it cannot be ignored that there is little doubt that the EU legislator found inspiration in the OECD Model when drafting the 1998 proposal and therefore included a BO requirement in the IRD. Because the BO concept was introduced in the 1998 proposal and subsequently only slightly modified in the final IRD (except for the specific BO requirement for PE's; *see* above sub 5.2.1), we believe that the 1996 OECD Model served as inspiration for the IRD's BO concept. Hence, only the 1996 OECD Model and its Commentary can serve as an additional source to interpret to IRD's BO requirement. However, it should be borne in mind that the OECD Model and the OECD Commentary are nothing more than legally non-binding recommendations of the OECD's Committee on Fiscal Affairs. The general interpretation methods of EU law to interpret an ambiguous term should always prevail.

The CJEU is of the opinion that the OECD Model and Commentary after the 1996 version are also relevant when interpreting the IRD's BO concept. If we take the various developments as regards the clarification of the OECD's BO concept into account, this implies that the IRD's BO concept is subject to a dynamic interpretation. It is not the first time that the CJEU applies a dynamic use of the OECD Commentary.[180] In *Berlioz*, the CJEU used the 2012 OECD Commentary on Article 26 OECD Model to interpret a concept included in the 2011 Directive on Mutual Assistance.[181, 182]

The foregoing implies that the interpretation given by the OECD to the BO concept in the OECD Commentary thus becomes legally binding through the IRD. This is

[177] CJEU, 26 Feb. 2019, IRD-case, § 90.
[178] Opinion AG Kokott, 1 Mar. 2018, *N Luxembourg 1*, C-115/16, § 55.
[179] CJEU, 26 Feb. 2019, IRD-case, § 92 with reference to §§ 4 to 6.
[180] CFE, *supra* n. 43, at 17.
[181,] CJEU 16 May 2017, *Berlioz*, C-682/15, §§ 66–67.
[182] Council Directive 2011/16/EU of 15 Feb. 2011 on administrative cooperation i taxation and repealing Directive 77/799/EEC.

remarkable because the OECD Commentary is, unlike the double tax conventions concluded by contracting states, a non-binding international instrument.[183] This also implies that the OECD has de facto legislative powers within the EU because it influences the interpretation of the IRD's BO concept.[184] The applicants in the IRD-case argued that this is not acceptable because the OECD lacks any democratic legitimacy. In our opinion, this argument is rightfully made because the OECD Model and the OECD Commentary are drafted and revised by the OECD's Committee on Fiscal Affairs, whose decisions are not approved by legislative bodies. The CJEU, however, countered this argument by stating that the basis of the BO concept still lies in the IRD itself and that its legislative history reflects the democratic process of the EU.[185] This counterargument of the CJEU is regrettable because it is too easy as it ignores the fact that nowhere in the IRD or its legislative history any reference is made that supports the interpretation of the BO concept in the IRD in accordance with the OECD Model and Commentaries. Also, it does not really address the concerns of the applicants.

Whilst the CJEU states that OECD Commentary published after the 1996 OECD Model are relevant to interpret the BO concept, it should be noted that it does not (explicitly) rely on the 2014 OECD Commentary.[186] This is remarkable because the referring court explicitly referred to the 2014 OECD Commentary in one of the BO related questions.[187] Furthermore, it is even more remarkable that the CJEU implicitly referred to the 2014 OECD Commentary when listing all indicators of abuse (*see* above sub 4.1.).[188] This seems to suggest that the CJEU relied on the 2014 OECD Commentary when interpreting the concept of abuse while it did not when interpreting the IRD's BO concept.

No explanation is given why the CJEU did only explicitly rely on the 1997 Commentary and 2003 Commentary, and not on the 2014 Commentary. Is this because the 2003 Commentary was already published (i.e. on 28 January 2003) when the IRD was adopted (i.e. on 4 June 2003)?[189] Or can it be explained by the fact that the disputes relate to interest payments in the years 2006 to 2009? Or did the CJEU not rely on the 2014 Commentary to interpret to BO concept because it first concluded that the EU's concept refers to an economic concept (*see* above sub 5.3.1) whilst the 2014 Commentary narrowed down the OECD's BO concept to recipients who are obliged to pass on the income (*see* above sub 5.1)? Or is it none of those and just a mere oversight?

Although the CJEU clarified that the OECD Model and OECD Commentaries '*are relevant*' when interpreting the IRD's BO concept, it is not clear what this relevance exactly means. For example, it is currently not clear how 'dynamic' the IRD's BO concept should be interpreted, i.e. which versions of the OECD Commentary are relevant. Should one take the date of the interest payment into account when determining which version of the OECD Commentary is relevant as the absence of reference to the 2014 Commentary may suggest?

Because the CJEU explicitly stated that OECD Commentary published after the 1996 OECD Model are relevant to interpret the IRD's BO concept and that we should not be concerned about the lack of the democratic legitimacy of the OECD at EU level, we believe that one should also take the 2014 and 2017 OECD Commentary into account, irrespective of the date of the interest payments. These versions of the OECD Commentary are clarifications and elaborations of the 2003 OECD Commentary.[190] Indeed, the OECD Public Discussion Draft notes that

> *the concept of "beneficial owner" found in Articles 10, 11 and 12 of the OECD Model Tax Convention has given rise to different interpretations by courts and tax administrations. Given the risk of double taxation and non-taxation arising from these different interpretations, the OECD Committee on Fiscal Affairs (…) has worked on proposals* ***aimed at clarifying the interpretation*** *that should be given to that concept in the context of the OECD Model Convention* (authors underline).[191]

This would imply that the IRD's BO concept has an autonomous EU law meaning, but that it should be used in a narrow technical sense and not as a wide anti-abuse provision and that it is to be interpreted in accordance with the 2014 OECD Commentary. Hence, a taxpayer who receives an interest payment and uses this to repay a loan or pay off his debts towards suppliers, employees etc. (*see* our example above sub 5.4.1) qualifies as BO unless he would be bound by a legal or contractual obligation to pass on the interest received to another person.[192]

On the other hand, one could be pragmatic, like Gutmann, and argue that the fact that the CJEU does not refer to the 2014 OECD Commentary does not really matter since the CJEU refers to that Commentary when determining whether a conduit company abuses the IRD (*see* above sub 4.1.).[193] However, while that is true, still this is an implicit reference only to that part of the OECD Commentary that deals with an interposed

183 Introduction, § 29, OECD Comm. 2017.
184 Ottosen & Andersen, *supra* n. 173, at 3–4.
185 CJEU, 26 Feb. 2019, IRD-case, § 91.
186 CJEU, 26 Feb. 2019, IRD-case, § 92 does not refer to § 7. In § 7 the legal context is given and there the 2014 OECD Commentary is mentioned as part of that context.
187 CJEU, 26 Feb. 2019, IRD-case, § 45.
188 CJEU, 26 Feb. 2019, IRD-case, §§ 128–33.
189 O. Marres, *Panta rhei: de doorstroomarresten*, 6 Nederlands Tijdschrift voor Fiscaal Recht Beschouwingen 4 (2019).
190 Baker, *supra* n. 136, at 95.
191 OECD Public Discussion Draft of 29 Apr. 2011 on the clarification of the meaning of 'beneficial owner' in the OECD Model Tax Convention, 2.
192 Baker, *supra* n. 136, at 93.
193 D. Gutmann, *Contre la théorie du bénéficiaire effectif en droit fiscal européen et international*, 2 Fiscalité Internationale 2 (2019).

company that has no dependent contractual or legal obligations to pay on what it received, but does so 'in substance'.

5.4.3 *PSD's Implicit BO Requirement*

In the PSD-case the CJEU ruled that the benefits of the PSD are refused if the BO of the dividends is resident in a third state (irrespective whether there is any fraud or abuse of rights).[194] The CJEU says to find support for this conclusion based on the aim of the PSD, i.e. the avoidance of double taxation of dividend distributions within the EU.[195] Scholars have therefore argued that the CJEU reads an implicit BO requirement in the PSD.[196]

In our view, another reading of the abovementioned dictum by the CJEU is possible. The CJEU made this dictum when addressing the question of the referring court whether abuse of rights is possible where the BO of the dividends – BO being the term used by the Danish court that refers to the person who receives the dividends that flow through an abusive conduit company – is tax resident in a third state with which the source Member State has concluded a double tax treaty according to which no withholding tax would be due if the dividends were directly paid from the source Member State to the BO in the third state.[197] In this question, the BO concept seems to refer to the OECD's BO concept included in the applicable double tax treaty between the third state and the source Member State. Hence, when the CJEU refers to the term BO in the following paragraphs of its judgments, that term should also be understood as referring to OECD's BO concept. A similar issue arose in the *Parts Service* case, where the CJEU addressed the question whether abuse involves a transaction having as 'principal' or 'sole' aim obtaining a tax advantage. The CJEU clarified that it referred to the 'sole' aim of a transaction in *Halifax* because in that case the referring national court found that there was no business purpose for the abusive transaction at stake and that the sole aim was to claim full VAT recovery.[198] This implies that the question asked by the referring court is important to understand the terminology used by the CJEU.

When addressing the question of the referring court, and as already discussed sub 4.1, the CJEU observes that it is possible that a company located in a third state (that has concluded a double tax treaty with the source Member State under which a withholding tax exemption is available when the dividends would have been received directly by a recipient in this third state) interposes a group company located in a Member State without such group structure qualifying as abuse of rights.[199] If the BO of the dividend is a resident in a third state the refusal of the PSD's benefits is not subject to fraud or abuse of rights.[200] Because the PSD does not contain a BO requirement, one could argue that the CJEU implicitly addresses the situation of a direct dividend distribution to the BO in the third state. In such situation, the refusal of the PSD's benefits is obvious as the scope of application of the PSD is limited to companies (and PEs) that are tax residents in Member States. Fraud or abuse is not relevant for that discussion as the CJEU rightfully observes.

Furthermore, in the discussion on the burden of proof of abuse of rights, the CJEU also mentions the BO concept several times. Such has also led authors to conclude that the PSD contains an implicit BO requirement.

First, in paragraph 117 of its judgment, the CJEU states that the tax authorities should evidence an abusive practice taking into account all relevant factors, in particular the fact that the company that receives the dividends does not qualify as BO. It is not surprising that the CJEU refers to the BO concept because the abusive practices in the case at hand relate to conduit companies (that do as a matter of principle not qualify as BO), and the BO concept is also mentioned in the various indicators of abusive practices (*see* above sub 4.1). In this paragraph of the judgment, the CJEU thus refers to the BO concept as one of the indicators of abuse, and not as an implicit BO requirement to the PSD.

Second, the CJEU ruled in paragraph 120 of its judgment that a Member States' tax authorities are not required to identify the BO of a dividend when they refuse to grant a company the status of BO or where abuse is established. From this dictum, one could also derive that the PSD contains an implicit BO requirement because the CJEU makes a clear distinction between the burden of proof of the BO requirement and the burden of proof of abuse (*see* above sub 4.2). However, we believe that this would be an unjustified conclusion. The answer of the CJEU in paragraph 120 addresses the question of the referring court whether the PSD requires the Danish tax authorities to establish the (true) BO once they have proven that the conduit company receiving the dividend is an abusive practice. Therefore, once again the CJEU uses the term BO of the dividend in its answer as that is the term used in the question referred to it by the Danish Court. As discussed earlier sub 4.2, the CJEU answers that question negatively. In any event, it is difficult to see how the fact that the BO notion suddenly pops-up in part of the discussion on the burden of proof of an abusive practice under the PSD could mean that the PSD contains an implicit BO requirement.

Finally, as already mentioned under sub 5.2.1, the CJEU ruled in *Denkavit* that a condition to apply the PSD is to be interpreted strictly because such condition

[194] CJEU 26 Feb., PSD-case, § 111.
[195] CJEU 26 Feb., PSD-case, § 113.
[196] CFE *supra* n. 43, at 12; Haslehner & Kofler, *supra* n. 64; Gutmann, *supra* n. 192, at 1–2; Marres, *supra* n. 188, at 5.
[197] CJEU 26 Feb., PSD-case, § 107.
[198] CJEU 21 Feb. 2008, C-425/06, *Part Service*, § 44.
[199] CJEU 26 Feb. 2019, PSD-case, § 110.
[200] CJEU 26 Feb. 2019, PSD-case, § 111.

constitutes a derogation from the principle of withholding tax exemption.[201] Taking this case law into account, we believe that the CJEU cannot add an additional condition to the benefits of the PSD without any sufficient legal basis. Hence, we believe that the CJEU cannot add an implicit BO requirement to the PSD. Moreover by adding such condition to the PSD the CJEU would violate the principle of legal certainty.

In view of the above, we are of the opinion that the benefits of the PSD are not subject to an implicit BO requirement. We hope that the CJEU will clarify this in its future case law.

6 Relationship between BO and the Abuse of Rights Principle

6.1 Two Sides of the Same Coin?

The BO concept and abuse of rights principle are intertwined in the analysis of the CJEU in the IRD-case and PSD-case.[202] The CJEU, however, does not clarify the exact relationship between these two concepts, more in particular whether BO is to be regarded as a specific form of tax abuse in the sense of the abuse of rights principle.

By way of introduction, it should first be noted that the OECD's BO concept is assumed to be an anti-avoidance rule.[203] As from the 2014 OECD Commentary it is clear that BO is a narrow anti-avoidance rule that targets a specific form of tax avoidance through the interposition of an intermediary who is obliged to pass on the income received to someone else.[204] Hence, the degree of substance of the BO is immaterial (*see* above sub 5.1).[205] Other types of tax abuse (in particular treaty shopping through conduit companies) are dealt with by other provisions in the OECD Model, such as the LOB provision and PPT, the latter being a general anti-avoidance rule (GAAR) for which substance could play an important role (*see* above sub 4.1).[206]

It is debatable whether the IRD's BO concept is a specific anti-abuse provision or merely a condition to apply the IRD. Because the IRD contains a separate provision as regards the prevention of fraud and abuse (Article 5 IRD), one could argue that the BO requirement to the IRD is merely a condition to apply the IRD. The fact that the CJEU holds that the recipient of the interest has the duty to establish that he is the BO (*see* above sub 4.2) confirms that view. On the other hand, it could also be argued that the BO requirement aims to tackle the interposition of intermediaries that wrongfully want to obtain the benefits of the IRD, which leads to the conclusion that the BO requirement is indeed a specific anti-abuse provision. The European Commission seems to adhere to this position because it assumes a connection between the BO concept and the CJEU's anti-abuse case law (*see* above sub 5.2.1). Initially this was a rather semantical discussion. However, as from the emergence of the EU law principle prohibiting abuse in the case law of the CJEU the outcome of this discussion has become very relevant.

The reasoning of the CJEU in the PSD- and IRD-cases as regards the relationship between the BO requirement and the abuse of rights principle is confusing. On the one hand, the Court explicitly refers to the BO requirement in its analysis of the constituent elements of abuse in case of a conduit company (*see* above sub 4.1).[207] Furthermore, it ruled in connection with the burden of proof that when the tax authorities of a Member State refuse the benefits of the IRD and PSD, they should prove that all elements of an abusive practice are fulfilled while taking into account all relevant factors including, and in particular, whether the recipient of the income is the BO (*see* above sub 4.2).[208] The CJEU clearly makes a connection between the BO requirement and the abuse of rights principle and seems to argue that the BO requirement is a specific aspect of the abuse of rights principle. This would imply that the BO requirement falls under the broader abuse of rights principle.

On the other hand, from other dicta in the PSD- and IRD-cases one could also derive that the CJEU clearly assumes that BO and the abuse of rights principle are two distinct concepts. For example, in the context of the burden of the proof, the CJEU makes such clear distinction ('*to refuse to accord a company the status of beneficial owner […],* ***or*** *to establish the existence of abuse*', authors underline).[209] Several scholars also refer to the dictum of the CJEU according to which the benefits of the IRD or PSD are refused if the BO is a resident in a third state irrespective whether there is any fraud or abuse of rights.[210] However, as the BO concept in this paragraph arguably refers to the OECD's BO concept (*see* above sub 5.4.3), one cannot rely on this paragraph to uphold that both notions are distinct. Finally, it should also be noted that the AG Kokott opined that the BO concept and abuse of rights doctrine are distinct concepts.[211]

In our view, the BO concept and abuse of rights doctrine are indeed two distinct concepts. First, the purpose of both concepts is different. The BO requirement aims to ensure that the IRD's benefits are granted

[201] CJEU 17 Oct. 1996, C-283/94, *Denkavit*, § 27.
[202] J. Schwarz, *Beneficial Ownership: CJEU Landmark Ruling*, Kluwer International Tax Blog (27 Feb. 2019), http://kluwertaxblog.com/2019/02/27/beneficial-ownership-cjeu-landmark-ruling/.
[203] Art. 1, § 63 OECD Comm.
[204] Art. 10, § 12.5 OECD Comm.
[205] Baker, *supra* n. 136, at 101.
[206] Art. 29, § 187 OECD Comm.
[207] CJEU 26 Feb. 2019, PSD-case, §§100- 104, IRD-case, §§ 127–31.
[208] CJEU 26 Feb. 2019, PSD-case, §117, IRD-case, § 142.
[209] CJEU 26 Feb. 2019, PSD-case, §120, IRD-case, § 145; *see also* Marres, *supra* n. 188, at 4–5.
[210] CFE, *supra* n. 43, at 18; Haslehner & Kofler, *supra* n. 64; Marres, *supra* n. 188, at 5.
[211] Opinion AG Kokott, 1 Mar. 2018, *N Luxembourg 1*, C-115/16, § 60.

to the person entitled to the income. It is therefore a condition for the taxpayer to rely on the Directive, i.e. an objective test to assess whether a taxpayer is entitled to the Directive's benefits. The abuse of rights doctrine, on the other hand, serves as a general principle of EU law and has a different function (*see* above sub 3.3). With respect to the IRD, it operates subsequently to the testing of whether the formal conditions of this directive are met and aims at denying the benefits of the IRD once it has been established that the scheme abuses the provisions of the IRD (*see* above sub 3.2.2).

Furthermore, when the IRD was drafted the European Commission considered it necessary to include a BO requirement and a separate reservation of competence to strike down abuse (Article 5 of the IRD) in the IRD. If the BO concept would be a corollary of this anti-avoidance provision, it would have been redundant to also include a separate BO requirement in the IRD.

Finally, the fact that the IRD's BO concept has an autonomous definition that is independent from the abuse of rights principle is also an argument to support that both concepts are distinct. Indeed, notwithstanding the fact that the definition of the IRD's BO concept is not crystal clear, it is clear that it does not include an objective and subjective element like the general EU law principle on the prohibition of abuse of rights does. If this would have been the case, the CJEU definitely would have made this clear in the IRD-case when addressing the questions as regards the BO concept. However, the CJEU does not refer to the general principle prohibiting abuse or to an alleged objective of prevention of abuse that would be pursued by the BO definition at all when discussing the meaning of BO.

Although BO and the abuse of rights doctrine are distinct, it is clear from the CJEU's analysis that there is an overlap between these two concepts. There are indeed situations where the recipient of an income does not qualify as BO and that also qualify as tax abuse. This is typically the case when an intermediary company is used with the sole purpose to obtain the IRD's benefits where such company does not benefit economically from the income because it is obliged to pass it on to another person that for whatever reason does not qualify for the benefits under the IRD. Such situation could thus be caught under the BO requirement and the abuse of rights doctrine. However, there are obviously also situations where only one of the concepts is present, i.e. a situation where the recipient of the income does not qualify as BO but that is not deemed abusive (e.g. the Swiss swaps case where a Danish bank was deemed not to qualify as the BO of a Swiss dividend whilst the situation did not qualify as abuse[212]), or a situation that is deemed abusive whilst the recipient of the income qualifies as BO (e.g. the sale by a parent company of the usufruct of shares of its subsidiary for a period of three years in order that the buyer (a financial institution) is able to receive dividends free from withholding tax (while dividends received by the seller would be subject to withholding tax) and the seller reiceves an amount that corresponds to the present value of the dividends)[213].

In the cases discussed here the BO concept and the abuse of rights doctrine are intertwined because of the underlying facts, i.e. the Danish tax authorities argued that the third State residents interposed conduit companies in order to wrongfully rely on the withholding tax exemptions in Denmark under the IRD and PSD and that those third State residents were the BO's.[214] Because the referring court therefore asked various questions to the CJEU in relation to the BO concept and the abuse of rights doctrine, it is not surprising that the CJEU deals with both together, as is clearly illustrated by the various indicators of abuse (*see* above sub 4.1). We believe that this would be different if the underlying facts were different, e.g. a situation that is deemed abusive without the BO requirement being discussed over vice versa.

6.2 Practical Implications

6.2.1 *Absence of BO Requirement in Domestic Law (in the Absence of Abuse of the PSD or IRD)*

The first and arguably most important implication following the fact that the BO requirement does not qualify as an anti-abuse test, is that it obviously cannot be invoked by the tax authorities of a Member State with reference to the general EU law principle on the prohibition of abuse of rights.

For the IRD, a Member State is entitled to require from a company the proof that it qualifies as BO of the interest or royalties.[215] This supposes that the Member State has transposed the IRD's BO requirement in its domestic tax laws. If the Member State has chosen not to do so and transposed the IRD in a more lenient manner, it is not possible for the tax authorities to add a BO requirement to the IRD's benefits (principle of inverse direct effect, estoppel; *see* above sub 3.2.2). In order to rely on the general EU law principle prohibiting abuse of rights, the tax authorities should establish that a situation qualifies as abuse of the IRD, i.e. that the objective and subjective element are both fulfilled. Such evidence is not available when a recipient of an income merely does not qualify as BO. Consequently, in the absence of a domestic transposition of the IRD's BO requirement a mere paying agent could for example benefit from the withholding tax exemption of the IRD

[212] CH: Tribunal Fédéral, 7 Mar. 2012, *A. v. Eidgenössische Steuerverwaltung* ESTV, A-6537/2010, IBFD research portal.

[213] Compare to Art. 29, § 182 OECD Comm. example B. We assume that the financial institution is not bound by a contractual or legal obligation to pass on the dividend and thus implicitly qualifies as BO.

[214] CJEU 26 Feb. 2019, PSD-case, § 102, IRD-case, § 129.

[215] CJEU 26 Feb. 2019, IRD-case, § 140.

(assuming that the other conditions to apply the IRD are fulfilled).

If one assumes that the PSD does not contain an implicit BO requirement (*see* above 5.4.3), the benefits of the PSD can arguably never be subject to a BO requirement. For the reasons just explained, a Member State's tax authorities cannot deny the PSD's benefits because the recipient does not qualify as BO while relying on the abuse of rights principle. Moreover, we believe that a Member State is even prevented from denying the PSD's benefits when the recipient allegedly does not qualify as BO. In our view, a Member State cannot add a BO requirement to the PSD as a domestic or agreement based anti-abuse provision (Article 1 (2) of the PSD). First this would go against the settled case law that Member States cannot add conditions where the Directive does not provide so. And secondly, adding a provision on ground of the prevention of abuse should have as specific objective the prevention of wholly artificial arrangements which do not reflect economic reality, the purpose of which is to unduly obtain a tax advantage.[216] As said before sub 6.1, the BO requirement is an objective test to assess whether a taxpayer is entitled to the IRD's benefits and has nothing to do with wholly artificial arrangements. It is therefore unlikely that the BO concept complies with the requirements developed by the CJEU as regards the abuse concept. We note that AG Kokott opined that the BO requirement in the dividend article in a double tax treaty cannot be deemed a transposition an agreement-based anti-abuse provision in order to deny the benefits of the PSD.[217]

6.2.2 *Alternative Relief*

What are the consequences of the finding by the tax authorities of a Member State that an interposed conduit company does not qualify as BO under the IRD or that it abuses the IRD or PSD?:

A. Interposed conduit company does not qualify as BO (in the absence of abuse)

In the IRD-case the CJEU explicitly clarified that the mere fact that a recipient is not the BO of an interest or royalty payment does not necessarily mean that the IRD's withholding tax exemption is not applicable. If the BO of the income is established in the EU and satisfies all other conditions to apply the IRD, the withholding tax exemption can still be applied.[218] In practice, such situation could for example occur when Company 1 located in Member State A makes an interest payment to a 'sister' Company 2 in Member State B. If the common parent Company 3 of the payer (Company 1) and recipient (Company 2) of the interest payment is located in Member State C and it qualifies as the BO of the interest payment, it can benefit from the IRD provided that all other conditions are fulfilled. This means that Member State A is obliged to grant the withholding tax exemption. The CJEU arguably found inspiration in the OECD Commentary, according to which the limitation of source State taxation remains available when an intermediary is interposed between the beneficiary and the payer of an interest payment, if the beneficiary is the BO and all other relevant conditions are fulfilled (*see* above sub 5.1).[219]

If Company 3 in this example would be a resident in a third state, it can clearly not rely on the IRD because the scope of application of the IRD is limited to companies (and PE's) located in a Member State of the EU. However, in such situation, we believe that Company 3 should be able to rely on a double tax treaty between Member State A and the third state, if any, and consequently benefit from the limitation of source State taxation under that treaty, provided that, in addition to Company 3 being the BO of the interest, all conditions required to apply the relevant treaty provision are fulfilled. The OECD Commentary explicitly foresees this possibility.[220]

In the PSD-case the CJEU did not make any similar statements because the PSD does not include a BO requirement (*see* above sub 5.4.3). For purposes of applying the PSD, it is as a matter of principle irrelevant whether the recipient would qualify as BO in the meaning of the IRD's BO concept or the OECD's BO concept. However, as explained above sub 4.1, not being the BO could be an indicator for abuse.

B. Interposed conduit company is an abusive practice

The consequences of the finding that a certain situation qualifies as abusive, are different. First, it should be noted that the CJEU did not explicitly address these consequences in the judgments of 26 February 2019. From its judgment in *Halifax*, however, it follows that an abusive transaction is to be redefined in order to re-establish a situation that would have prevailed in the absence of the abusive transaction. The judgment is grounded on the general EU law principle of proportionality.[221] This implies that one should requalify a certain situation for tax purposes in such a way as if the tax abuse did not occur. This is the only way to do justice to the aim of applying the abuse of rights principle. Authors confirm that in case of abuse the proper remedy is to reduce the effects of the abusive conduct to the proper (i.e. non abusive) conduct. If not, one would impose the sanction of fraud which is the complete

[216] CJEU 7 Sept. 2017, *Eqiom*, C-6/16, § 30; CJEU 20 Dec. 2017, *Deister Holding*, joined cases C-504/16 and C-613/16, § 60.
[217] Opinion AG Kokott, 1 Mar. 2018, *T Danmark*, C-116/16, § 106.
[218] CJEU 26 Feb. 2019, IRD-case, § 94.
[219] Art. 11, § 11 OECD Comm.
[220] Art. 11, § 11 OECD Comm.
[221] CJEU, 21 Feb. 2006, *Halifax*, C-255/02, §§ 92 et seq. The CJEU repeated this doctrine in CJEU, 22 Dec. 2010, C-103/09, *Weald Leasing*, §§ 48 and 52.

elimination of the benefits fraudulently claimed plus a penalty (deterrent effect) and such would be dispropotional.[222] Imagine that Company 1 in Member State A holds the shares in Company 2 located in Member State B, but interposes a newly established Company 3 located in Member State C that allows the tax-free upstreaming of dividends from Company 2 to Company 1. If this interposition of Company 3 is qualified as abuse of the PSD, under the *Halifax*-doctrine a dividend distributed by Company 2 is for tax purposes deemed to be received by Company 1, i.e. the original shareholder of Company 2. The dividend will be added to the taxable base of Company 1.

It is unclear whether the PSD or the IRD can still be applied after the redefinition of an abusive practice. Imagine that Company 1 (95%) and Company 2 (5%) are resident in Member State A and hold their respective participations in Company 3 located in Member State B. Member State B levies a domestic withholding tax of 25% on dividend distributions, and only provides for a withholding tax exemption in accordance with the PSD in case of a 10% direct shareholding. Company 1 and Company 2 decide to interpose a newly established Company 4 in Member State C because this Member State does not require a minimum shareholding for the withholding tax exemption of the PSD to be applicable. Hence, a dividend distributed by Company 3 can be upstreamed to Company 1 and Company 2 (through Company 4) without any withholding tax leakage. If this arrangement is deemed abusive, the dividend payment by Company 3 is redefined as if it was made directly to Company 1 and Company 2. We believe that Company 1 could then rely on the PSD in order to obtain a withholding tax exemption because the situation should be re-defined as if no tax abuse occurred. In such a situation Company 1 could also rely on the PSD. Moreover, the CJEU clarified in *Halifax* that the finding of an abusive practice may not lead to a penalty, for which a clear and unambiguous legal basis is necessary.[223] If the withholding tax exemption of the PSD is denied to Company 1 after redefinition of the transaction its situation would be worse compared to the situation when no abuse had occurred. Hence, the finding of the abusive practice would penalize Company 1 where the benefits of the PSD would be refused. This would not in line with *Halifax* and the principle of proportionality underlying that judgment.

Assuming that Company 1 could rely on the PSD, the questions arise how far the redefinition of the abusive situation goes. If only the dividend distribution is redefined, the conditions of the PSD would not be fulfilled because Company 1 does not hold the shares in Company 3 directly. If the dividend distribution and the shareholding are redefined, this would imply that Company 1 is deemed to hold Company 3 directly. Hence, Company 1 could rely on the PSD (assuming that the other conditions are also fulfilled). We believe that the redefinition implies that Company 1 is deemed to hold the shares in Company 3 directly and receives the dividend from Company 3. This is logical because one cannot assume that Company 1 would receive a dividend from Company 3 whilst it does not hold the shares in Company 3.

In our example, after redefining the abusive practice, Company 2 would also be deemed to hold its shareholding in Company 3 directly and receive a dividend from Company 3. However, it cannot rely on the PSD because it does not hold a participation of at least 10% as is required by Member State B. Hence, the redefinition of the abusive situation results in the denial of the withholding tax exemption for the dividend deemed distributed to Company 2. Let us now assume that Member State A and Member State B concluded a double tax treaty that provides for a reduced withholding tax of 10% irrespective the size of the participation, the question arises whether Company 2 could rely on this double tax treaty to enjoy a reduced withholding tax in Member State B. According to certain scholars this would not be possible based on the EU law principle of sincere cooperation (Article 4 (3) TEU).[224] However, we believe that the *Halifax*-doctrine enables Company 2 to rely on the double tax treaty. If no abuse had occurred, Company 2 could also have relied on this double tax treaty. Moreover, the denial of the treaty benefits would result in a penalty for Company 2 contrary to that doctrine and violate the principle of proportionality.

The same issues arise for companies located in a third state. Imagine that Company 1 is located in a third state A, and holds Company 2 located in Member State B. Member State B levies a domestic withholding tax on dividend payments of 25%, that can be reduced under the A-B double tax treaty to 10%. Company 1, however, interposes a newly established Company 3 located in Member State C because the A-C double tax treaty provides for a withholding tax exemption, and the PSD applies in relation to a dividend distributed by Company 2 to Company 3. Hence, a dividend distributed by Company 2 can be upstreamed to Company 1 without any withholding tax leakage. If the interposition of Company 3 is qualified as abusive the situation should be redefined as if no abuse occurred, i.e. Company 1 is deemed to hold Company 2 directly and to receive the dividend from Company 2. In such a scenario, in

[222] A. Lenaerts, *The Relationship Between the Principles of Fraus Omnia Corrumpit and of the Prohibition of Abuse of Rights in the Case Law of the European Court of Justice*, Com. Mkt. L. Rev. 1712 (2011).

[223] CJEU, 21 Feb. 2006, *Halifax*, C-255/02, § 92–93.

[224] L. C. van Hulten & J. J. Korving, *Svig og Misbrug: The Danish Anti-Abuse Cases*, Intertax 799–800 (2019). Upon adoption of the PSD GAAR a similar question was raised by Debelva and Luts who are of the opinion that the application of the PSD GAAR does not prevent a taxpayer to rely on a double tax treaty in order to obtain 'equivalent benefits' (F. Debelva & J. Luts, *The General Anti-Abuse Rule of the Parent-Subsidiary Directive*, ET 231–32 (2015)). Weber, on the other hand, argues that this would violate the principle of sincere cooperation (Weber, *supra* n. 100, at 104–05).

accordance with the *Halifax*-doctrine, we believe that Company 1 can rely on the A-B double tax treaty in order to reduce the withholding tax levied by Member State B from 25% to 10%. If no abuse occurred, Company 1 would also have been able to rely on the A-B double tax treaty. Furthermore, following that doctrine the application of the general principle of the prohibition of abuse cannot result in a penalty (i.e. the denial of the application of the A-B double tax treaty) and should be proportionate.

In practice, however, there could be issues to apply the direct tax Directives or a double tax treaty. The fact that according to the CJEU the tax authorities are not required to establish the BO when abuse is proven (*see* above sub 4.2) may preclude taxation as if no abuse has occurred. This is in clear contradiction with the CJEU's judgment in *Halifax*. Even if one admits that in certain cases it may be difficult for the tax authorities to know the precise identity of the BO's, the exact amount of income that they will receive or have received and when receipt occurs, we believe that the *Halifax*-doctrine and the general EU law principle of proportionality require the tax authorities to give alternative relief in the State of source. If the taxpayer has provided the tax authorities with the undisputed evidence of the identity of the BO's, the amount of income that they have received and the timing of that receipt, the BO should be entitled to obtain alternative relief, subject of course to the situation where the State of source would be time barred to make the alternative assessments or refunds under applicable statute of limitations-rules

6.3 Has the BO-Concept Become Obsolete?

When the BO concept was introduced in the IRD, there was limited case law of the CJEU in the field of (tax) abuse. Meanwhile the CJEU's case law in that area has steadily developed towards the upholding of a general principle of EU law that prohibits abuse of EU law and the judgments in the PSD- and IRD-cases show that there is a certain overlap between the BO concept and the concept of abuse as they can apply simultaneously in certain situations, e.g. where a conduit company is interposed in order to wrongfully obtain the benefits of the IRD (*see* above sub 6.1). One may therefore wonder whether the BO concept has become obsolete. Gutmann is of that opinion and has argued that the BO concept should be deleted from the IRD and that the IRD should be amended, like the PSD in 2015, to include a GAAR.[225]

Because the concept of BO and the abuse of rights principle are fundamentally different (e.g. different conditions to apply, burden of proof, consequences, etc.), we believe that the BO concept is still useful. More in particular, the BO concept is useful to deny the IRD's benefits in situations that do not qualify as abuse but where the recipient is bound to pass on the income in accordance with a contractual or legal obligation. In that regard, it would be useful to include a BO requirement in the PSD, which would also end the confusion on whether a BO requirement is implicitly included in the PSD (*see* above sub 5.4.3). While there is no absolute need to include a GAAR in the IRD given the presence of the general principle of the prohibition of abuse in EU law (*see* above sub 3.3), we agree with Gutman that from the perspective of legal certainty, it would be a wise policy to copy the PSD-GAAR into the IRD as the contours of abuse are better expressed in a technical provision than in a general principle of law and coherence between the two Directives would be achieved.[226] Additionally one could leave the IRD untouched and prevent its abuse under the ATAD GAAR. In any event, the reservations of competence according to which Member States are free to decide to introduce measures to prevent abuse of the direct tax Directives, should be deleted because they are overruled by the CJEU's judgments of 26 February 2019 (*see* above sub 3.3).

The fact that the BO concept is still useful does not mean that there are no issues. In an EU context, the interpretation of the IRD's BO concept remains ambiguous. This ambiguity even increased by the statements of the CJEU in the IRD-case, in particular regarding the use of the OECD Commentary (*see* above sub 4.4.2). We therefore hope that the CJEU will clarify the meaning of the IRD's BO concept in its subsequent case law because a clear definition is a *conditio sine qua non* for its usefulness and correct application.

7 Conclusion

With the judgments of 26 February 2019, the Grand Chamber of the CJEU added a new chapter to the history of tax abuse. In this contribution, we analysed these judgments as regards the abuse of rights principle and the BO concept. It follows from our analysis that there are still many open questions to be answered with respect to these topics, in particular how far the abuse of rights principle reaches (*see* above sub 3.5) and whether the PSD includes an implicit BO requirement (*see* above sub 5.4.3). On the other hand, there are also many open questions as regards these topics that were not at stake in these judgments, such as the effect of the CJEU's interpretation of the BO concept on double tax treaties between Member States and between a Member State and a third state, and the application of the abuse of rights principle from the perspective of the Member State where a conduit is located. Because there are still many open questions to be answered, the Danish BO cases will certainly not be the last chapter in the history of tax abuse.

[225] Gutmann, *supra* n. 192, at 3.

[226] For the same reason, a mandatory GAAR should be included in the MD unless it is preferred to prevent abuse under the ATAD GAAR.