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Does Avoidance of Member State's Tax Justify Hindrance of  
Treaty Freedoms?

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## **ABBREVIATIONS**

COJ, Court	European Court of Justice
TFEU, Treaty	Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, <i>Official Journal of the European Communities</i> (May 2008) C 115.
OECD	Organisation for Economic Co-operation and Development.
CFC	Controlled Foreign Corporation

# 1. INTRODUCTION

## 1.1 Purpose

The importance of common language has been recognized by the human race since the dawn of history. This basic truth is even more important when it comes to the legal field, which pretends to direct behavior. As Professor John Tiley, a prominent British scholar admonishes judges '[t]heir words are pored over not just for the fun of gazing at entrails but in order to give advice about what those very judges might do next.'<sup>1</sup> and 'What is vital is that the courts should be honest in their reasoning'<sup>2</sup>. This rule seems not to have been observed by the COJ in its rulings on the compatibility of Member State's anti tax avoidance measures with the Treaty.

The research question I would like to examine in this paper is – Does avoidance of Member State's tax justify hindrance of treaty freedoms?

My research hypothesis, which I will try establish in this paper, is that though this kind of justification existed in the past in the Court's case law, it was silently abolished in the *Cadbury Schweppes* case.<sup>3</sup> I will try to demonstrate that, despite the fact that this justification still exists to this day in the Court's discourse, it has become a dead letter.

## 1.2 Method and Material

The research, which led to the writing of this paper, was initiated by identifying the COJ's cases in which the tax avoidance prevention justification for Treaty freedoms breaches was implemented. I chose these cases because they relate directly to the research question of this paper. Since in these cases the Court uses in its analysis the same tests used to identify prohibited abusive behavior, I went on to identify the COJ cases in which the abuse of law principle was implemented.

In reading the COJ cases I implemented Professor John Tiley's advice to 'bypass the judicial rhetoric in particular cases and ask what the judges have actually done'.<sup>4</sup>

In order to identify the common thread in these cases I took assistance from the scholarly literature dealing with the tax avoidance prevention justification and the abuse of law principle.

In order to support the claims brought up in this paper with regard to the COJ jurisprudence, I chose to adopt an historical approach, reviewing the case law development. This approach is specifically required in light of the multiple scholarly approaches existing with regard to the construction of the COJ's case law in the topics at hand.

## 1.3 Delimitation

The inconsistency of the COJ case law in the development of the abuse of law principle of interpretation and the prevention of tax avoidance justification for Treaty freedoms breaches stimulated much legal writing. Basic questions, such as the scope of these doctrines, their

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<sup>1</sup> B. Arnold, "A Comparison of Statutory General Anti-Avoidance Rules and Judicial General Anti-Avoidance Doctrines as a Means of Controlling Tax Avoidance: Which is Better? (What Would John Tiley Think?)", in J. Jones, P. Harris, D. Oliver, eds., *Comparative Perspectives on Revenue Law-Essays in Honour of John Tiley* (2008), 1-24, 3.

<sup>2</sup> *Idem*, 6.

<sup>3</sup> Case C-196/04 *Cadbury Schweppes, PLC v. Inland Revenue* [2006] ECR I-7995.

<sup>4</sup> Arnold, 6.

substance, and their interrelations are not agreed upon by scholars, and can not be ascertained before further clear case law is issued by the COJ.<sup>5</sup> Therefore, the legal situation in the EU as it is described in this paper should be understood to represent only the authors understanding and not as the agreed point of view on these issues, as such does not exist.

The case law and the scholarly literature surveyed in this paper hardly represent all which were scanned in the research process and certainly not all that have been written on these topics. In order to keep this paper to the point I chose to review in it only what I believe are the most important pieces of legal literature needed for answering the research question. In that regard, this paper will not deal with anti-abuse or anti-avoidance provisions incorporated in the different EU law legislation, except for when it is required for clarifying the development of the general anti-abuse principle in the COJ case law, as these are not required to answer the research question examined in this paper.

#### **1.4 Disposition**

The organizing of this paper is straightforward. It starts with general definition of the notions 'tax avoidance' and 'abuse of law', together with background information about their role in the EU legal order before being implemented in the COJ case law. The two following chapters describe the parallel development in the COJ case law of the tax avoidance prevention justification and the abuse of law principle of interpretation. The analysis of the *Cadbury Schweppes* case, which follows, aims at presenting the practical merger of these two doctrines, which caused the abolition of the tax avoidance prevention justification. The COJ case law after *Cadbury Schweppes* with regard to the tax avoidance prevention justification will then after be reviewed in order to substantiate the practical abolition of that justification. Chapter 6 will conclude.

## **2. BASIC NOTIONS -TAX AVOIDANCE AND ABUSE OF LAW**

### **2.1 Tax Evasion, Tax Avoidance, and Tax Planning**

There is no universal definition for "tax avoidance", but it is customary to define it as a form of illegal tax dodging, distinct from another form of illegal tax dodging which is "tax evasion". Although both forms of behavior cause loss of revenue for the fisc,<sup>6</sup> the distinction between these two is important since tax evasion, as opposed to tax avoidance, usually bears criminal consequences for the involved taxpayer (or, more accurately, the endeavoring non-taxpayer).<sup>7</sup>

The difference between these two forms of behavior is that while "evasion" escapes the tax payment without escaping the liability, consequently breaking the law, "avoidance" tries to escape the liability of the tax.<sup>8</sup> In other words, while tax evasion is clearly illegal, tax avoidance illegal merits are discovered only *a posteriori*. The clear illegality of tax evasion usually indicates that the taxpayer has consciously and deliberately decided to disregard the law, and hence the presence of criminal intent, whereas in cases of tax avoidance there will be sufficient uncertainty so that no criminal intention could be inferred.<sup>9</sup>

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<sup>5</sup> P. Pistone, "Italy: The 3 M Italia Case (C-417/10)" (*not yet published*), 121-137, 132.

<sup>6</sup> C. Pinto, *Tax Competition and EU Law*, Vol. 7, EUCOTAX Series on European Taxation (2003), 49.

<sup>7</sup> P. Merks, "Tax Evasion, Tax Avoidance and Tax Planning", *INTERTAX* 34:5 (2006): 272-281, 273.

<sup>8</sup> A. Gunn, "Tax Avoidance" *Michigan Law Review* 76 (April 1977): 733-767, 734.

<sup>9</sup> Pinto, 58-59.

The distinction between "tax evasion" and "tax avoidance" behaviors stems from the different character of the norms which underlay their prohibition. While tax evasion is prohibited by clearly defined laws, tax avoidance is usually prohibited by flexible standards, which requires a case-by-case ruling. Standards, as opposed to clear-cut laws, contain leeway for the tax authority discretion to *ex post* determine whether a tax scheme, despite *prima facie* observance of the law, is prohibited. Standards are being used in order to enable the tax authority flexibility in guarding the fisc, because experience shows that any clear-cut rule will ultimately be avoided by taxpayers. It should be noted that if an activity which has been denounced as tax avoidance under a standard is repeated, by the taxpayer involved in the prior denunciation or others, it is tax evasion and not tax avoidance, as its illegality has become clear and unambiguous.<sup>10</sup>

Within tax evasion a distinction is sometimes being made between omission offences and offences which require action, such as false declaration or fake invoices.<sup>11</sup> The latter are considered more serious and sometimes described as 'tax fraud'.

Another distinction that should be made is between "tax avoidance" and "tax planning". The notion tax planning refers to the use of legal means for tax liability reduction,<sup>12</sup> in contrast to tax avoidance which is illegal. The distinction between these two forms of tax mitigation is based on a borderline drawn by the relevant tax jurisdiction. That is why some scholars prefer to distinguish between "acceptable tax avoidance" and "unacceptable tax avoidance" which is parallel to the distinction between "tax planning" and "tax avoidance".<sup>13</sup>

As a general rule, the larger the scope of anti-avoidance measures within a tax jurisdiction, the harder it is to claim that a meaningful distinction can be drawn between tax avoidance and tax planning. That is also true in the opposite situation, where there are no anti-avoidance measures taken by the tax jurisdiction.

While the majority of tax jurisdictions allow taxpayers to arrange their affairs in a way that attracts minimum tax liability, most will not allow a taxpayer to contrive artificial transactions, i.e. transactions which are solely or mainly tax driven and/or conflict with the aim of the tax legislation, to reduce tax that is otherwise payable. In this manner tax jurisdictions observe the neutrality of their tax systems<sup>14</sup> and prevent economic inefficiency.<sup>15</sup>

Tax avoidance can take the form of tax deferral, or temporary tax saving, and permanent tax saving. Tax deferral is *de facto* income deferral, since the deferral is caused by income deferral. The longer the period of a tax temporary tax saving, the more valuable it is for the taxpayer and the harder it is to distinguish it from a permanent tax saving.<sup>16</sup> The existence of multiple tax jurisdictions creates many tax avoidance opportunities for taxpayers, as they may take advantage of the disparities in tax legislation by allocating income and assets to related taxpayers in another, lower tax, jurisdiction. An example for a tax deferral scheme in that

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<sup>10</sup> Merks, 276.

<sup>11</sup> *Idem*, 273.

<sup>12</sup> J. Prebble, "Abus de Droit and the General Anti-Avoidance Rule of Income Tax Law: A Comparison of the Laws of Seven Jurisdictions and the European Community" (2008).  
<<http://www.victoria.ac.nz/sacl/cagtr/working-papers/WP56.pdf>>

<sup>13</sup> Merks, 274.

<sup>14</sup> Generally speaking, neutrality in a fiscal system means that no distortions or loss of efficiency is caused by the imposition of taxes so that taxpayer business decisions are not affected by tax considerations.

<sup>15</sup> Pinto, 52.

<sup>16</sup> *Idem*, 65.

regard is the use of CFC as conduit between the income source and the taxpayer. Transfer pricing and thin capitalization are examples for tax saving schemes.<sup>17</sup>

## 2.2 Prevention of Member States Tax Avoidance in the EU

International tax avoidance prompted countries to legislate unilateral anti-avoidance measures and to seek collaborations with other countries in the fight against tax avoidance, both through bilateral tax treaties and the framework of supranational organizations.<sup>18</sup> A 1975 European Council Resolution<sup>19</sup> recognized the harms caused by international tax evasion and tax avoidance practices and called for collaboration, both within the EU and with third countries, in order to hinder it. The Resolution also stated that the European Commission will take appropriate steps, within the scope of its powers, in that regard. This report prompts the adoption, two years later, of the Mutual Assistance Directive<sup>20</sup> which aims at strengthening the collaboration between tax administrations within the EU in order to hinder practices of tax evasion and tax avoidance.

As will be displayed in this paper, the COJ takes a different approach from the Commission, the Council, and the Member States, as it refuses to take the Member States tax base preservation interests into consideration in its rulings, hence again and again striking down the Member States anti avoidance legislation which is not in accordance with the Treaty freedoms.

Lately, the European Council adopted a Resolution<sup>21</sup> which provides recommended guidelines for Member States when applying cross-border CFC and thin capitalisation rules within the EU which are not applicable in similar domestic situations. This coordination measure could be understood as an outcome of the Member States dissatisfaction from the COJ strict approach to their anti avoidance legislation.

## 2.3 Abuse of Law

In some countries, tax avoidance is perceived as a form of 'abuse of law' (sometimes called 'abuse of rights') or '*abus de droit*'. This terminology refers to any use or claim of private right which exceeds the limits of its reasonable use and enforcement.<sup>22</sup>

The doctrine of abuse of law was developed by the French jurisprudence in the *Clément Bayard* case. The case concerned a landowner who had erected a fence consisting of metal spikes around his boundaries in order to prevent hot-air balloons, taking off in a nearby airfield, from flying over his property. The landowner brought a claim against a balloonist who had his balloon punctured by the fence, draped, and in landing caused damage to the fence. The balloonist counterclaimed against the danger created by the spikes on the fence.

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<sup>17</sup> L. Faulhaber, "Sovereignty, Integration and Tax Avoidance in the European Union: Striking the Proper Balance", *Columbia Journal of Transnational Law* 48:2 (2010), 1-71, 7-9.

<sup>18</sup> OECD, *International Tax Avoidance and Evasion, Four related studies* (Paris, 1987), 11.

<sup>19</sup> Council Resolution of 10 February 1975 on Measures to be taken by the Community in Order to Combat International Tax Evasion and Avoidance, *Official Journal of the European Communities* (February 1975) C 35.

<sup>20</sup> Council Directive 77/799/EEC of 19 December 1977 Concerning Mutual Assistance by the Competent Authorities of the Member States in the Field of Direct Taxation, *Official Journal of the European Communities* (December 1977) L 336. Later amended in Council Directive 2004/56/EC of 21 April 2004 amending Directive 77/799/EEC concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation, certain excise duties and taxation of insurance premiums, *Official Journal of the European Communities* (April 2004) L 127.

<sup>21</sup> Council Resolution of 8 June 2010 on coordination of the Controlled Foreign Corporation (CFC) and thin capitalisation rules within the European Union, *European Communities* (June 2010) C 156.

<sup>22</sup> Prebble, 18.

The French Court of Cassation ruled in favor of the balloonist, arguing that the fence was erected in order to harm the property owner's neighbor, constituting abuse of the right of ownership.

The abuse of law doctrine is known only in civil law countries and is alien to common law countries, such as the United Kingdom or Ireland. Also among civil law countries the scope of the doctrine is not uniform and has different meanings.<sup>23</sup> Some examples to the implementation of the doctrine with regard to tax law in the legal systems of some prominent Member States, or the replacements used in its absence, will be provided hereinafter.

In France the abuse of law doctrine is incorporated in Article L 64 of the French Tax Code. This paragraph empowers the French tax administration to disregard transactions that are constructed solely for the purpose of providing tax benefits. The tax administration's authority to disregard transactions exists even if the formal elements of the transactions are effective in law. The implementation of this authority involves a complicated and highly observed administrative procedure.<sup>24</sup>

In Germany the abuse of law doctrine is incorporated in Section 42 of the German Federal Code. It provides that a taxpayer may not arrange his affairs inadequately.<sup>25</sup>

Inadequacy exists where:

- (1) an objective third party, in the same circumstances and with the same economic purpose as the taxpayer, would not have proceeded as the taxpayer did; and
  - (2) the arrangement concerned had the effect of reducing tax liability; and
  - (3) there are no important reasons to suggest that the inadequate legal arrangement is reasonable and justified by non-economic or other important considerations; and
  - (4) the arrangement have been chosen with the actual intention or motive of reducing tax.
- The existence of this element is presumed where of the first three objective requirements exist.

Where abuse of law is found to exist, tax is re-calculated and charged as if the taxpayer had chosen an adequate legal arrangement.

As abovementioned, the United Kingdom lacks a general anti-abuse of law rules. However, its courts have developed a substitute judicial doctrine in order to control tax avoidance. The anti-avoidance case law is based on contextual and purposive interpretation of the relevant tax legal provisions in order to determine if a transaction is within its statutory purpose.<sup>26</sup>

From the above presentation it can be concluded that in the civil law countries tax avoidance is being curtailed using a *motive test*, which examines the taxpayers' intentions. On the other hand, in common law countries, it is being done using a *purposive interpretation*, which examines the relevant tax provision's scope. This distinction will prove to be important when we come to examine the development of the abuse of law principle in the COJ's case law.

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<sup>23</sup> Confédération Fiscale Européenne, C.F.E. Opinion Statement on General Anti-Avoidance Rules as submitted to the Council, the European Commission and the European Parliament (2005); Merk, 276.

<<http://old.tax.org.uk/attach.pl/1729/3931/07-2005%20Anti%20Avoidance.pdf>>

<sup>24</sup> Prebble, 20-21.

<sup>25</sup> *Idem*, 5-6.

<sup>26</sup> *Idem*, 41; Arnold, 21.



After clarifying the above basic notions, we shall now start the journey, which will end with answering the research question, by examining the development of the prevention of tax avoidance justification up to the revolutionary *Cadbury Schweppes* case.

### 3. THE EARLY DEVELOPMENT OF THE TAX AVOIDANCE JUSTIFICATION

#### 3.1 The Treaty Freedoms protection Jurisprudence

A common market means the abolition of obstacles to the free movement of good, persons, services and capital between the Member States.<sup>27</sup> Therefore, Member State's direct tax measures may be in conflict with the TFEU if it restricts the free movement of goods,<sup>28</sup> the free movement of persons (which includes the free movement of EU citizens,<sup>29</sup> the free movement of workers,<sup>30</sup> and the freedom of establishment),<sup>31</sup> the freedom to provide services,<sup>32</sup> or the freedom of capital and payment circulation.<sup>33</sup>

The Court case law developed a three-prong test in order to assess the compatibility of Member State's direct tax measures with the TFEU freedoms.<sup>34</sup>

First to be tested is the presence Treaty standing,<sup>35</sup> i.e. whether the situation enters into the scope of the TFEU provisions. In order to enjoy Treaty protection two conditions must be fulfilled:

- (i) the situation must come within the ambit of one of the freedoms.
- (ii) the relevant situation must involve a cross-border activity, as opposed to an activity which takes place only within the borders of one Member State (an internal situation). Cases of cross-border activities involving a Member State and a non-EU State are given Treaty access only where it relates to the freedom of capital and payment circulation, as the rest of the TFEU freedoms apply in intra-EU situations alone.

After Treaty standing has been established, the Court examines the presence of discriminatory or restrictive treatment. These concepts are quite broad and relate both to overt and covert discrimination or restriction.

Discrimination consists of treating differently comparable situations, with the consequence that one of the situations is subject to a worse treatment, or treating alike different situations. As one Member State nationals and other Member States nationals are generally considered to be in a comparable situation, a cross-border situation involving other Member States national should be treated the same as a purely internal situation.<sup>36</sup>

A restriction, on the other hand, refers to non-discriminatory hindrance to the use of the Treaty freedoms. All measures which prohibit, impede or render less attractive the exercise of the Treaty freedoms are regarded as restrictions. When it comes to tax legislation, a treatment may be considered restrictive even if the cross-border situation is only subject to more burdensome procedural or administrative requirements with comparison to the internal one.<sup>37</sup>

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<sup>27</sup> M. Helminen, *EU Tax Law – Direct Taxation* (2009), 55.

<sup>28</sup> Article 34 TFEU.

<sup>29</sup> Article 21 TFEU.

<sup>30</sup> Article 45 TFEU.

<sup>31</sup> Article 49 TFEU.

<sup>32</sup> Article 56 TFEU.

<sup>33</sup> Article 63 TFEU.

<sup>34</sup> Pinto, 303.

<sup>35</sup> B. Terra, P. Wattal, *European Tax Law - fifth edition* (2008), 32.

<sup>36</sup> Helminen, 49.

<sup>37</sup> *Idem*, 57-58.

In the *Daily Mail* case<sup>38</sup> the COJ confirmed that the Treaty, even though mostly directed at precluding restrictions imposed by a Member State on other Member States nationals activities in its territory, also prohibit the application of direct tax measures which result in restrictions on the use of TFEU freedoms by the relevant Member State own nationals (home state restrictions), e.g. anti tax avoidance measures.

Nonetheless, restrictive or even discriminatory measures may be enacted if there is a justification in the form of a mandatory requirement of public interest overriding the need to ensure the TFEU freedom.<sup>39</sup> There are two groups of such justifications. The first group contains the “written” justifications, enacted in Articles 52, 62 and 65 TFEU. These statutory justifications may allow discrimination or restriction of the TFEU freedoms, for example, on the grounds of public health, public order or public security. The second group consist the “unwritten” justifications, recognized by the COJ under the so-called rule of reason which was developed in the landmark *Cassis de Dijon* case.<sup>40</sup> These justifications are based on overriding public interest requirements that the Court considers protection worthy even though they hinder the Treaty freedoms.

It is important to stress that according to COJ case law the unwritten justification can only justify a restrictive and not discriminatory measures. Discrimination, on the other hand, can only be justified based on the written justifications. The reason for this distinction is that restrictive measures are considered less harmful to the Treaty freedoms, as they only impose more burdensome conditions for a freedom exercise, as oppose to discriminatory measures which prevent its realization all together. Nevertheless, there has been continues erosion in the Court position in that regard, so that in many recent judgments discriminatory measures can be found justified based on the Court's rule of reason.<sup>41</sup>

In order for a justification to be applicable, it is necessary that the tax measure concerned is both:

- (i) Appropriate to achieve the justified goal, i.e. the justified goal could be achieved by the measure.
- (ii) Proportionate, i.e. the justified goal could not be achieved by less restrictive measures and the restriction is not unreasonable in comparison to the justified goal.

### **3.2 The Tax Avoidance Justification and its Narrowing Down**

The COJ has accepts the need to prevent the avoidance of Member State's tax legislation as a possible justification for restrictive measures, based on the rule of reason.<sup>42</sup> Nevertheless, in 1998 the Court began a process narrowing down this justification,<sup>43</sup> until it was practically abolished in the wake of *Cadbury Schweppes* case. The Court used the proportionality analysis for that end, restricting the scope of this justification to cases where the anti-avoidance measure applied only to '*wholly artificial arrangements*'. The Court's case law in that regard will be described hereinafter up to the rendering of the *Cadbury Schweppes* judgment, which will be dealt with separately together with its successors.

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<sup>38</sup> Case 81/87 *The Queen v. Daily Mail and General Trust plc* [1988] ECR 5483, para. 16.

<sup>39</sup> Pinto, 305.

<sup>40</sup> Case 120/78 *Rewe-Zentrale v. Bundesmonopolverwaltung für Branntwein* [1979] ECR 649.

<sup>41</sup> Pinto, 303-304.

<sup>42</sup> Faulhaber, 15.

<sup>43</sup> Lilian, 18.

The phrase “wholly artificial arrangements” first appeared in the *Imperial Chemical Industries (ICI)* case.<sup>44</sup> ICI was a UK company holding 49% in another UK company. The latter holding company owned the shares of 23 subsidiaries, of which 4 were established in the UK, 6 in other EU countries, and 13 in non-EU countries. Under UK tax law, resident companies owning at least 90% of the shares in other resident trading companies were entitled to offset the operating losses of their subsidiaries against their own income. The same rule applied to the holding companies shareholders. This consortium relief was limited to cases where no more than 25% of the subsidiaries held by the UK holding company were established outside the UK. Based on the consortium relief, ICI sought to offset its relative part in the losses of one of the UK subsidiaries against its own taxable income. However, the UK tax administration denied ICI the application of the consortium relief, since the majority of the holding company's subsidiaries were established outside the UK. ICI claimed that the consortium relief limitation had the effect of hindering the freedom of establishment.

After accepting ICI argument, the Court dismissed the UK claim for justification, which was also based on the need to prevent the risk of tax avoidance by domestic taxpayers' schemes meant to shift foreign losses to UK entities and profits outside the UK. The Court reasoned its decision based on the proportionality principle, stating:<sup>45</sup>

"the legislation at issue ... does not have the specific purpose of preventing *wholly artificial arrangement*, set up to circumvent United Kingdom tax legislation, from attracting tax benefits, but applies generally to all situations...".

Furthermore, the Court stressed that the consortium relief limitation was also not appropriate to achieve its goal, as the risk of loss and profit shifting was also present if the holding company had only one foreign subsidiary, a situation in which the limitation would have not applied and the consortium relief would have been granted to ICI.

The Court continued to implement the 'wholly artificial arrangement' doctrine in the cases that followed, e.g. *Lankhorst-Hohorst GmbH*,<sup>46</sup> *Rewe Zentralfinanz eG*,<sup>47</sup> striking down Member State's anti-avoidance measures. In some cases the COJ, despite striking down the challenged anti-avoidance measure, proposed changes that would make the measure proportionate, and hence sustainable.<sup>48</sup>

Only in one case in which the Court implemented the 'wholly artificial arrangement' doctrine prior to *Cadbury Schweppes* was a Member State's anti-avoidance measures recognized as justified by the COJ. This case is the *Marks & Spencer* case.<sup>49</sup>

It concerned a UK tax legislation which allowed resident companies in the same group to set off profits and losses against one another. The group relief was denied with regard to group companies not resident in the UK.

Marks & Spencer claimed the group relief with regard to losses incurred by its subsidiaries which were established in Belgium, Germany and France. The claims for the group relief were rejected by the UK tax authorities on the ground that group relief could only be granted

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<sup>44</sup> Case C-264/96 *Imperial Chemical Industries (ICI) v. Kenneth Hall Comler (Her Majesty's Inspector of Taxes)* [1998] ECR I-4695.

<sup>45</sup> *Idem*, para. 26.

<sup>46</sup> Case C-324/00 *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt* [2002] ECR I-11779.

<sup>47</sup> Case C-347/04 *Rewe Zentralfinanz eG v. Finanzamt Köln-Mitte* [2007] ECR I-2647.

<sup>48</sup> Case C-9/02 *Hughes de Lasteyrie du Saillant v. Ministère de l'Économie, des Finances et de l'Industrie* [2004] ECR I-2409; Case C-451/05 *Européenne et Luxembourgeoise d'investissements SA (ELISA) v. Directeur général des impôts and Ministère public* [2007] ECR I-08251; Case C-105/07 *Lammers & Van Cleeff NV v. Belgisch Staat* [2008] ECR I-00173.

<sup>49</sup> Case C-446/03 *Marks & Spencer v. Halsey* [2005] ECR I-10837.

for losses recorded in the UK. The COJ concluded that the group relief denial constitutes a restriction on the freedom of establishment. Nevertheless, the Court was willing to consider the restriction as justified due to the need to protect a balanced allocation of the power to impose taxes between the different Member States, the danger that losses would be used twice, and the risk of tax avoidance, taken together,<sup>50</sup> as long as the group relief was also provided with regard to other Member States subsidiary's losses when the following two criteria were met:<sup>51</sup>

- The non-resident subsidiary has exhausted the possibilities available in its State of residence of having the losses taken into account for the accounting period concerned by the claim for relief and also for previous accounting periods, if necessary by transferring those losses to a third party or by offsetting the losses against the profits made by the subsidiary in previous periods; and
- There is no possibility for the foreign subsidiary's losses to be taken into account in its State of residence for future periods either by the subsidiary itself or by a third party, in particular where the subsidiary has been sold to that third party.

The next major development in the Court's attitude towards Member State's anti avoidance measure occurred in the *Cadbury Schweppes* case, where new meaning was ascribed to the notion 'wholly artificial arrangement'. But in order to clarify what has been done by the Court in the ambit of *Cadbury Schweppes*, we must first move to describe the development of the abuse of law principle of interpretation in the Court's case law, and its establishment as an *a priori* condition for the granting of Treaty standing.

#### **4. THE DEVELOPMENT OF THE ABUSE OF LAW PRINCIPLE**

##### **4.1 Overview**

Over the past decades the number of appearances of the notion 'abuse of law' in the COJ case law has been growing exponentially. But the development in the use of this notion is not only quantitative but also qualitative. Abuse of law, which was first used in COJ case law on Treaty freedoms as a justification in the three-prong test, latter became an independent *a priori* test for the incidence of EU law, i.e. Treaty standing. The substance of the test behind this notion has also evolved over the years, and so did the scope of incidences in which it was applied.

It is seems that in its contemporary rulings the COJ treats abuse of law as a principle of interpretation, used in all fields of EU-law, to examine the incidence of EU law. An abuse of law practice can be found to exist if two requirements are fulfilled:

- (1) Despite formal application of an EU law right, the result of the underlying behavior is contrary to the purpose of the provision granting the right; and
- (2) It is apparent, from a number of objective factors, that the essential aim for the underlying behavior is to obtain an improper goal.

This doctrine is not without its problems. It appears to be generally acceptable that a "general principle" of EU law can be elaborated by the COJ when it applies in most (but not necessary all) Member State.<sup>52</sup> In order to be able to claim that abuse of law is a general principle of EU

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<sup>50</sup> *Idem*, para. 51.

<sup>51</sup> *Idem*, para. 55.

<sup>52</sup> W. Lorez, "General Principles of Law: Their Elaboration in thr Court of Justice of the European Communities" *American Journal of Comparative Law* 13:1(1964): 1-29, 7-9.

law which applies in most Member States, the COJ unified for the sake of its abuse of law doctrine the motive test, which is used in civil law countries to identify abuse of law, and the purposive interpretation of legal provisions, which is used in common law countries. But the result of this union is an absurd, as the concept abuse of law as it is construed by the COJ is not known in none of the prominent Member States.<sup>53</sup> Most of them implement one of the prongs of the test used by the COJ in that regard, i.e. the motive test *or* the purposive interpretation, but none of them implement them both.

To establish my distinctions above, the evolution of the abuse of law doctrine in the COJ case law will be reviewed hereinafter.

#### **4.2 Abuse of Law as an *a posteriori* Justification**

The first reference by the COJ to abuse of EU law was in the *Van Binsbergen* case.<sup>54</sup> The case involved the assessment of the compatibility with the freedom to provide services of a Dutch legal provision which held that only persons habitually resident in the Netherland could act as legal representatives before any appeal court. The Court found the Dutch legal provision to be not in accordance with EU-law, yet observed:<sup>55</sup>

“Likewise, a Member State cannot be denied the right to take measures to prevent the exercise by a person providing services whose activity is entirely or principally directed towards its territory of the freedom guaranteed by Article 59 for the purpose of avoiding the professional rules of conduct which would be applicable to him if he were established within that state...”

The above paragraph makes it clear that the Court treats the prevention of abuse of EU law as an *a posteriori* justification for a national anti abuse measure rather than an *a priori* test for the incidence of EU law.<sup>56</sup>

The *Kraus* case,<sup>57</sup> which then followed, examined the compatibility with Treaty freedoms of a German legal provision requiring academic titles acquired in foreign states, among them Member States, to be authorized by the competent ministry of the relevant land in order to be used in Germany. In regard to the German authorities claim, that the legislation at hand was designed to protect the public against misleading use of academic titles awarded outside the territory of the Germany, the Court made it clear that:<sup>58</sup>

“Community law does not preclude a Member State from adopting, in the absence of harmonization, measures designed to prevent the opportunities created under the Treaty from being abused in a manner contrary to the legitimate interests of the State”

By this the Court reaffirmed the abuse of EU law as a justification for national anti abuse measure.

Later, in the *TV10* case,<sup>59</sup> the Court implemented this justification. TV10 was incorporated in Luxembourg, but produced programs aimed primarily, but not exclusively, at audience in the Netherlands. The Dutch broadcasting authority, which imposed specific obligations on

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<sup>53</sup> See chapter 2.3 in this paper; Prebble.

<sup>54</sup> Case 33/74 *Johannes Henricus Maria van Binsbergen v. Bestuur van Bedrijfsvereniging voor de Metaalnijverheid* [1974] ECR 1229.

<sup>55</sup> *Idem*, para. 13.

<sup>56</sup> In other words, justification, by its nature, assumes that the Treaty standing terms exist. It is only an exception to the application of the Treaty that should have taken place in its absence.

<sup>57</sup> Case C-19/92 *Dieter Kraus v. Land Baden-Württemberg* [1993] ECR I-01663.

<sup>58</sup> *Idem*, para. 34.

<sup>59</sup> Case C-23/93 *TV10 v. Commissariaat voor de Media* [1994] ECR I-4795.

domestic broadcasters, wanted to impose these obligations on TV10 as well. TV10 argued that such obligations will infringe its freedom to provide services. The COJ ruled that:<sup>60</sup>

“The provisions of the EEC Treaty on freedom to provide services are to be interpreted as not precluding a Member State from treating as a domestic broadcaster a broadcasting body constituted under the law of another Member State and established in that State but whose activities are wholly or principally directed towards the territory of the first Member State, if that broadcasting body was established there in order to enable it to avoid the rules which would be applicable to it if it were established within the first state”.

This case is of particular interest due to the ideas expressed with regard to the abuse of law doctrine in the Opinion AG Lenz provided. First, he offers to restrict the application of the abuse of law justification to the freedom to provide services, claiming:<sup>61</sup>

"it is only within the framework of the freedom to provide services that the law of the country in which the services are provided can be applied under certain circumstances as a limitation of or an exception to the freedom as if the provider of services were established in that country"

Moreover, with regard to the question what constitutes an abusive behavior, he states:<sup>62</sup>

"Circumvention of a law or an abuse of law is regularly characterized by an intention to circumvent or abuse, which is undoubtedly a subjective factor. ... I regard the employment of subjective criteria for assessing the legally relevant conduct of a legal person as problematic. Consequently, I consider that the avoidance of legal provisions by a legal person should be able to be determined using objective criteria".

An objective form of the motive test to assess abuse of law, as offered by AG Lenz, was later accepted by the COJ in the *Halifax* case as part of a two prong test. But a series of judgments rendered then after in cases referred to the COJ by Greek courts, concerning alleged abuse of the Second Company Law Directive's provisions,<sup>63</sup> indicated the implementation of the abuse of law justification also to fields of EU law other than the freedom to provide services.

The *Kefalas* case<sup>64</sup> dealt with a the dispute concerning a Greek public limited company in financial distress whose management was taken over by a public body, with accordance to the Greek law, in order to re-organize it financially and bring it to recovery. In accordance with the special powers granted to it under national law, the public body increased the capital of the company without prior approval of the general shareholders meeting. The company's shareholders appealed against the decision, claiming that the capital increase was in breach of the Second Company Law Directive, which requires any capital increase in companies to be decided upon by the general shareholders meeting.

The Greek government considered the appeal as an abusive exercise of the right granted by Second Company Law Directive, and therefore sought to dismiss it based on Article 281 of the Greek Civil Code, a national anti-abuse provision which provides that "the exercise of a

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<sup>60</sup> *Idem*, para. 2.

<sup>61</sup> *Idem*, AG's Opinion, para. 33.

<sup>62</sup> *Idem*, para. 59 and 61.

<sup>63</sup> Second Company Law Directive 79/91/EEC of 13 Dec. 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second para of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with view to making such safeguards equivalent, *Official Journal of the European Communities* (December 1977) L 26/1.

<sup>64</sup> Case C-376/96 *Alexandros Kefalas and Others v. Elleniko Dimosio (Greek State) and Organismos Ikonomikis Anasinkrotisis Epikhiriseon AE (OAE)* [1998] ECR I-2843.

right is prohibited where it manifestly exceeds the bounds of good faith, morality or the economic or social purpose of that right".<sup>65</sup> The national court, based on various findings of fact, agreed with Greek government,<sup>66</sup> but was not sure if it may implement the national anti abuse measure with regard to a right granted by EU law.<sup>67</sup>

The COJ answered that a national court's authority to apply a domestic anti-abuse measure is restricted where it may prejudice the full effect and uniform application of EU law in that Member States by altering the scope of the relevant EU law provision or compromising the objectives pursued by it.<sup>68</sup> However, the Court found that EU law does not preclude a national court from examining whether the implementation of EU law right will cause improper advantage, manifestly contrary to the purpose of the relevant provision.<sup>69</sup> In other words, Member State's anti-abuse measures can be justified where a purposive interpretation of the EU law provision concerned indicates an abuse of EU law.

The *Diamantis* case,<sup>70</sup> which then followed, had very similar factual and legal background. It again dealt with a restriction of EU law right under the Second Company Law Directive by the Greek anti-abuse legislation. The COJ, referring to its prior rulings on the issue, restated that such national anti-abuse legislation may not prejudice the full effect and uniform application of EU law in the Member States. However, as EU law cannot be relied upon for abusive and fraudulent ends, that is to say in order to achieve an improper advantage manifestly contrary to the objectives of the relevant provision, the national courts may take into account such abuse in order to deny right granted under EU law.<sup>71</sup> The Court found the holding of the right claim in the case before it as an abuse not to compromise the uniform application and full effect of EU law, due to the disproportional damages expected to be caused to third parties as a result of the application of the claimed EU law right.<sup>72</sup>

It is interesting to indicate that while in the *Van Binsbergen* and *TV10* cases the motive test was used in order to identify an abuse of EU law (civil law originated) in the *Kefalas* and *Diamantis* cases abuse of law was identified using a purposive interpretation (common law originated). This seems to indicate the COJ's difficulties to formulate a unified abuse of law doctrine due to the different legal traditions of the Member States.

The Court kept referring to abuse of EU law as a possible justification for Member State's anti-abuse measures, and expanding the scope of fields of law to which it applied, in the *Centros* case.<sup>73</sup> *Centros Ltd* was incorporated under UK law and sought to trade in Denmark via a branch. The company was completely lacking substance in the UK. This construction was created in order avoid the Danish minimum capital requirements for company incorporation. The Danish authorities refused to register *Centros*'s branch due to the underlying avoidance cause. *Centros* appealed on the decision, basing its claim on the freedom of establishment.

The COJ began its analysis by stating that, in principle, Member States are entitled to take measures designed to prevent its nationals from avoiding domestic laws by exercising rights

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<sup>65</sup> *Idem*, para. 12.

<sup>66</sup> *Idem*, para. 13-14.

<sup>67</sup> *Idem*, para. 18.

<sup>68</sup> *Idem*, para. 21-22.

<sup>69</sup> *Idem*, para. 28.

<sup>70</sup> Case 373/97 *Dionysios Diamantis v. Elliniko Dimosio* [2000] ECR I-1705.

<sup>71</sup> *Idem*, para. 33-34.

<sup>72</sup> *Idem*, para. 43.

<sup>73</sup> Case C-212/97 *Centros v. Erhvervs – og Selskabssyrelsen* [1999] ECR I-1459.

granted by the Treaty.<sup>74</sup> However, the Court noted that despite the fact that the national courts may deny Treaty benefits, on a case by case base and only in situations in which there is objective evidence of the abuse or fraudulent conduct by the persons concerned, their final decision must take into account the objectives pursued by the EU law provisions concerned.<sup>75</sup> The Court did not find the fact that a company does not conduct any business in the Member State in which it has its registered office, and pursues its activities only in the Member State where its branch is established, sufficient to prove the existence of abusive or fraudulent conduct. Therefore, the Court concluded that Centros could not be denied of the benefit of the freedom of establishment.<sup>76</sup>

An interesting analysis, offering an innovative approach to abuse of EU law, was presented in AG La Pergola Opinion. It observed the following:<sup>77</sup>

“it is true that *the Court has consistently upheld in its case-law the principle that “rights conferred under Community law may not be relied on for fraudulent or abusive ends” which is among the general principles of Community law.* It is however by no means easy to define the precise scope of that principle. According to the recent judgment in Kefalas, a person abuses the right conferred on him if he exercises it unreasonably to derive, to the detriment of others, “an improper advantage, manifestly contrary to the objective” pursued by the legislator in conferring that particular right on the individual. On this aspect of the abuse of rights, there appears to be a certain affinity between the general principle regarding such abuse and the principle of proportionality as a criterion for limiting the exercise of power.

Furthermore, as learned authors have pointed out, the famous statement of the French authority on civil law, Planiol, that “law ceases where abuse begins” still holds good and shows very clearly that the problem of abuse is resolved in the last analysis by defining the material content of the particular situation and thus the scope of the right conferred on the individual concerned. *In other words, it is claimed that to determine whether or not a right is actually being exercised in an abusive manner is simply to define the material scope of the right in question.* If that is the case, I should like if I may revisit the ideas on freedom of establishment developed earlier (see points 13 and 16 above). That freedom certainly includes, for the purposes of the present case, the right to establish companies in accordance with the legislation of a Member State to carry on business in that State or, equally, in any other Member State. In other words, the newly formed company may set up its principal – and indeed its secondary – establishment wherever it wishes within the Community.”

The idea developed in AG La Pergola Opinion, that abuse of law is a general principle of EU law, and hence that abusive behavior falls outside of the scope of EU law, was adopted by the Court in the ground-breaking *Emsland-Stärke* case.<sup>78</sup> This case indicated the transformation of the abuse of law doctrine from a mere justification for Treaty freedoms hinderance to a Treaty standing requirement.

#### **4.3 Abuse of Law as an *a priori* General Principle of EU law**

*Emsland-Stärke GmbH*, a German company, exported potato-based products to Switzerland, for which it received export refunds under Regulation 2730/79.<sup>79</sup> Subsequently, it re-importing the same products into the EU, untouched and using the same means of

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<sup>74</sup> *Idem*, para. 24.

<sup>75</sup> *Idem*, para. 25.

<sup>76</sup> *Idem*, para. 29-30.

<sup>77</sup> *Idem*, AG's Opinion, para. 20.

<sup>78</sup> Case C-110/99 *Emsland-Stärke GmbH v. Hauptzollamt Hamburg-Jonas* [2000] ECR I-11569.

<sup>79</sup> Commission Regulation (EEC) No 2730/79 of 29 Nov. 1979 on the application of the system of export refunds on agricultural products, *Official Journal of the European Communities* (November 1979) L 317/1.



transportation, and paid the applicable customs duties. By doing so Emsland-Stärke tried to make gain from the positive difference between the export refunds it was entitled to receive and the applicable customs duties. Pursuant to an investigation by the German customs authorities Emsland-Stärke was required to repay the export refunds it received, a decision on which it appealed. The question the Court was essentially asked was whether, in these circumstances, Regulation 2730/79 should be interpreted as precluding Emsland-Stärke's right to export refund.

The Court answered, referring to its case law, that the scope of Community Regulations cannot be extended to cover abuses on part of a trader. Therefore, as the exportation and re-importation operations were not performed by Emsland-Stärke as bona fide commercial transactions, but only in order to wrongfully benefit from the grant of monetary compensatory amounts, it may be preclude from receiving the export refunds.<sup>80</sup> The Court then went on, stating that finding abuse of law requires:<sup>81</sup>

"...first, a combination of objective circumstances in which, despite formal observance of the conditions laid down by the Community rules, the purpose of those rules has not been achieved. ... second, a subjective element consisting in the intention to obtain an advantage from the Community rules by creating artificially the conditions laid down for obtaining it...."

The Court concludes that it is for the national court to examine the existence of these two elements in the instant case.<sup>82</sup>

The significance of the *Emsland-Stärke* ruling is triple. Firstly, for the first time the Court clearly indicated the criteria for determining the existence of abuse of EU law.<sup>83</sup> Secondly, in these criteria the Court united, to a one twofold test, the motive test and the purposive interpretation, previously used alternatively in its ruling to appreciate abuse. By doing so the Court gave regard to both civil law and common law traditional approaches to abuse of law/avoidance. Lastly, and most importantly, despite not making reference to abuse of law as a "general principle of Community law", the Court made it clear that such general principle exists, thus turning the abuse of law doctrine from an *a posteriori* justification, dependent for its application on the existence of anti-abuse measures in the national laws of Member State's, to an *a priori* independent Treaty standing condition. As a general principle of EU law abuse of law is also applicable by national courts, even in the absence of national anti-abuse legislation, due to their duty to implement interpretation consistent with that of the COJ.<sup>84</sup>

The abuse of law doctrine reached its current stage of development in the *Halifax* case.<sup>85</sup>

The case dealt with a scheme which involved a series of transactions between related parties, entered into for the sole purpose of enabling recovery of input VAT under the Common VAT System Directive,<sup>86</sup> which was not due in their absence. Halifax is a banking company, and as such its supplies are generally VAT exempt. For that reason its input VAT recovery rate is

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<sup>80</sup> *Emsland-Stärke GmbH v. Hauptzollamt Hamburg-Jonas*, para. 51.

<sup>81</sup> *Idem*, para. 52-53.

<sup>82</sup> *Idem*, para. 54.

<sup>83</sup> R. De La Feria, "Prohibition of Abuse of (Community) Law: The Creation of a New General Principle of EC Law Through Tax", *Common Market Law Review* 45:2 (2008): 395-441, 410.

<sup>84</sup> B. Terra, J. Kajus, *A guide to the European VAT Directives - Introduction to European VAT 2010* (2010), 83, 87.

<sup>85</sup> Case C-255/02 *Halifax and Others* [2006] ECR I-1609.

<sup>86</sup> Council Directive 2006/112/EC of 28 Nov. 2006 on the common system of value added tax, *Official Journal of the European Communities* (November 2006) L 347/1.

relatively low (at the relevant time it was only 5%). For the purpose of its banking business Halifax decided to construct call-centers. If it had purchased the construction services directly, little input VAT would have been recovered on the cost. In order to prevent this outcome, and enjoy full recovery of the input VAT incurred on the construction of the call-centers, it implemented a scheme which included a series of transactions involving three other related companies, each separately VAT registered.<sup>87</sup>

The COJ was asked, among other things, whether the doctrine of abuse of law, as developed in the Court case law, precludes a taxable person from exercising the right to deduct input VAT where the transactions underlying that right are effected for that exclusive purpose.

AG Poiares Maduro, in his Opinion, concluded that a general principle of interpretation prohibiting the abuse of EU law can be driven from the Court case-law.<sup>88</sup> Recalling the two prong test which was established in *Emsland-Stärke* in order to identify abuse of law,<sup>89</sup> the AG offered, in order to secure the nature of abuse of law as an interpretive principle, to convert the subjective prong of the test, the motive test, with an objective one. He offered to do so by changing the decisive elements in the motive test from the national court's appreciation of the relevant *mens rea* to a set of objective circumstances, verified in each individual case.<sup>90</sup>

To sum up its approach, the AG concluded that:<sup>91</sup>

"The Sixth Directive should be interpreted as not conferring on a taxable person the right to deduct or recover input VAT, in accordance with the Community law principle of interpretation prohibiting the abuse of Community law provisions, if two objective elements are found to be present in terms to be assessed by the national courts. First, that the aims and results pursued by the legal provisions formally giving rise to the right would be frustrated if the right claimed were actually conferred. Second, that the right invoked derives from activities for which there is no other explanation than the creation of the right claimed".

The Court confirmed in its judgment that the principle prohibiting abusive practices also applies in the sphere of VAT.<sup>92</sup> It then adopted the adjustment offered by the AG to the two prong test developed in the *Emsland-Stärke*, stating:<sup>93</sup>

"it would appear that, in the sphere of VAT, an abusive practice can be found to exist only if, first, the transactions concerned, notwithstanding formal application of the conditions laid down by the relevant provisions of the Sixth Directive and the national legislation transposing it, result in the accrual of a tax advantage the grant of which would be contrary to the purpose of those provisions.

Second, it must be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage. ... the prohibition of abuse is not relevant where the economic activity carried out may have some explanation other than the mere attainment of tax advantages".

The Court concluded that it is for the national court to verify in each specific case whether an abusive behavior has taken place.<sup>94</sup> If an abusive practice has been identified, the transactions

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<sup>87</sup> Terra, Kajus, 48.

<sup>88</sup> *Halifax and Others*, AG's Opinion, para. 64.

<sup>89</sup> *Idem*, para. 67.

<sup>90</sup> *Idem*, para. 71.

<sup>91</sup> *Idem*, para. 102.

<sup>92</sup> *Halifax and Others*, para. 70.

<sup>93</sup> *Idem*, para. 74-75.

<sup>94</sup> *Idem*, para. 76.

involved must be re-defined so as to re-establish the situation that would have prevailed in the absence of the transactions constituting that abusive practice.<sup>95</sup>

Some doubts with regard to the motive test, as re-defined in *Halifax*, have been clarified in the *Part Service* case.<sup>96</sup> In *Halifax* the Court claimed, in paragraph 75, that it must be apparent from a number of objective factors that the *essential* aim of the transactions concerned is to obtain a tax advantage. Nevertheless, later in the judgment, in paragraph 82, the Court seems to have changed its mind as it claimed that obtaining tax advantages was the *sole* purpose of the transactions at issue. In the *Part Service* the Court explained the different wording in this manner:<sup>97</sup>

“when it stated, in paragraph 82 of that judgment, that in any event, the transactions at issue had the sole purpose of obtaining a tax advantage, it was not establishing that circumstance as a condition for the existence of an abusive practice, but simply pointing out that, in the matter before the referring court in that case, the minimum threshold for classifying a practice as abusive had been passed.”

Consequently, the COJ held in *Part Service* that there could be a finding of an abusive practice under the motive test when the accrual of tax advantage constitutes the *principal* aim of the transaction or transactions at issue and not only if it is the *sole* purpose.<sup>98</sup>

It seems that the conversion of the motive test to an objective test in the *Halifax* case was preformed, firstly, in order to enable the Court more control over its application, and secondly, to prevent claims regarding the absence of abusive motive when a layman is acting base on professional advice.

It should be noted that while AG Poirares Maduro, in his Opinion in *Halifax*, offered to limit the incidents in which abusive motive could be inferred to "activities for which there is objectively no other explanation" the Court opt, both in *Halifax* and in *Part Service*, for the formula "essential aim" or "principal aim" of the transaction, widening significantly the scope of the motive test.<sup>99</sup>

The abuse of law principle took a somewhat different character in the case law which concerned the direct tax Directives, as will be reviewed hereinafter.

#### **4.4 The Abuse of Law Principle and the Direct Tax Directives**

The *Kofoed* case<sup>100</sup> dealt with an exchange of shears scheme under the Merger Directive.<sup>101</sup> The scheme involved the exchange of shears of a Danish company with the shears of an Irish company, both having the same Danish shareholders, in order to create a structure that will result in tax savings on dividends distributed to the final shareholders. The shareholders claimed in their tax returns that the exchange of shares should be exempt from tax, in

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<sup>95</sup> *Idem*, para. 95.

<sup>96</sup> Case C-425/06 *Ministerio dell'Economia e delle Finanze v. Part Service Srl* [2008] ECR I-897.

<sup>97</sup> *Idem*, Para. 44.

<sup>98</sup> *Idem*, Para. 45.

<sup>99</sup> De La Feria, 423.

<sup>100</sup> Case C-321/05 *Hans Markus Kofoed v. Skatteministeriet* [2007] ECR I-5795.

<sup>101</sup> Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, *Journal of the European Communities* (July 1990) L 225. Was latter amended by Council Directive 2005/19/EC of 17 February 2005 amending Directive 90/434/EEC 1990 on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States, *Journal of the European Communities* (March 2005) L 58/19.

accordance with the Merger Directive. The Danish tax authorities did not agree, taking the view that the exchange of shares should be taxed. The decision was challenged by the shareholders.

Article 11(1)(a) to the Merger Directive provides that a Member State may refuse to apply or withdraw Directive benefits where it appears that the exchange of shares has tax evasion or tax avoidance as its principal objective or as one of its principal objectives. Nevertheless, at the relevant time Article 11(1)(a) was not transposed into the Danish law.

Among other issues, the Court was required to answer whether in the absence of a specific transposition of Article 11(1)(a) of the Merger Directive its provision may still apply.

The Court, following the Opinion of AG Kokott, provided:<sup>102</sup>

"Article 11(1)(a) of Directive 90/434 reflects the general Community law principle that abuse of *rights* is prohibited. Individuals must not improperly or fraudulently take advantage of provisions of Community law. The application of Community legislation cannot be extended to cover abusive practices, that is to say, transactions carried out not in the context of normal commercial operations, but solely for the purpose of wrongfully obtaining advantages provided for by Community law."

In an answer to the abovementioned question, the Court provided that if there is in the national Danish law a provision or a general principle prohibiting abuse of rights, or other provisions on the prevention of tax evasion or tax avoidance which might be interpreted in accordance with Article 11(1)(a) of the Merger Directive, it may act to curb improper use of the Directive even though Denmark did not enact specific national measures aimed at implementing Article 11(1)(a) of the Merger Directive.<sup>103</sup>

The novelty of *Kofoed* is double. Firstly, the Court refers in it to the 'general Community law principle of abuse of *rights*' rather than 'abuse of *law*'. The Court did not only use different wording to label this principle, but also gave it different substance from the one given to the abuse of law principle in *Halifax*, claiming abusive behavior is examined solely based on the motive test in its subjective form. These differences led some scholars to believe that in *Kofoed* the Court introduced a different abuse principle.<sup>104</sup> Secondly, in contrast to its prior rulings, in *Kofoed* the Court required some transposing apparatus in the Member State national law in order for the 'abuse of rights' principle to be implemented by the national court. This approach could be explained by the presence of Article 11(1)(a) to the Merger Directive, which basically gives Member States the *option* to implement the abuse of right principle, hence subordinate the application of this general principle to transposition.<sup>105</sup>

We shall now move to examine the Court's judgment in the *Cadbury Schweppes* case, where the Court chose to implement the abuse of law principle in a surprising manner, that informed the abolition of the prevention of tax avoidance justification.

## 5. THE ABOLITION OF THE TAX AVOIDANCE JUSTIFICATION

The general principle of interpretation prohibiting abuse of EU law was implemented for the first time in the field of direct taxation in the *Cadbury Schweppes* case. Nevertheless much more significant for this paper analysis is the abnormal form in which this general principle

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<sup>102</sup> *Hans Markus Kofoed v. Skatteministeriet*, para. 38; AG's Opinion, para. 58.

<sup>103</sup> *Hans Markus Kofoed v. Skatteministeriet*, para. 46.

<sup>104</sup> De La Feria, 433.

<sup>105</sup> W. Schöen, "Abuse of Rights and European Tax Law", in J. Jones, P. Harris, D. Oliver, eds., *Comparative Perspectives on Revenue Law-Essays in Honour of John Tiley* (2008), 75-98, 78.

was implemented in this field, as it had the effect of abolishing the prevention of tax avoidance justification.<sup>106</sup> The Court, for reasons that will later be discussed, chose to conceal this tremendous effect, but in doing so undermined the legal certainty, and in the opinion of the writer of this paper, violated its basic duty to render a truthfully reasoned verdict.

Before moving on to analyze the *Cadbury Schweppes* case, a basic distinction between the general principle of interpretation prohibiting abuse of law and the prevention of tax avoidance justification should be clarified. While the former aims to prevent *EU law* from being misused, the latter is directed at preventing *national tax laws of Member States* from being circumvented by taking advantage of the provisions of EU law.

This different focus, the interests of *EU law* when it comes to the abuse of law principle and the interests of *national tax laws of Member States* when it comes to the tax avoidance justification, together with the fact that the principle of abuse of law has a general *a priori* effect as oppose to a justification which has an *a posteriori* effect, entails, necessarily, that the latter should have a wider scope, or else it is meaningless. This basic logic was not observed by the COJ in the *Cadbury Schweppes* case, in which the scope of these two elements was equaled, hence causing the practical abolition of the prevention of tax avoidance justification.

### 5.1 *Cadbury Schweppes*

Cadbury Schweppes, a company registered in the UK, was the parent company of the Cadbury Schweppes group which consisted, among others, two subsidiaries in Ireland. These subsidiaries performed the intra-group lending treasury activities, hence enabling the Cadbury Schweppes group to benefit from the low Irish corporate income tax rate.

The UK's CFC regime provided that for UK tax purposes this construction had to be ignored, ascribing the profits of the subsidiaries to Cadbury Schweppes and taxing it according to the UK tax rate. The purpose of the CFC legislation was to prevent erosion in the UK's tax base, caused by profits transfers from UK companies to subsidiaries in other States which applies a much lower tax rate than that in effect in the UK.

The COJ was asked whether the UK's CFC regime is compatible with the freedom of establishment. This required the Court to answer possibly three sub-questions:

- (i) Does the establishment of a subsidiary in another Member State for the purpose of enjoying a more favorable tax regime constitute an abuse of the freedom of establishment? Does this behavior grants Treaty standing?
- (ii) If necessary - does the UK's CFC regime hinders the freedom of establishment?
- (iii) If necessary - can that hindrance be justified?

AG Léger starts in his analyses with the abuse of law question. Explaining the relations between the motive test and the purposive interpretation in the two prong test, he states:<sup>107</sup>

"according to case-law, when the objective pursued by freedom of establishment is fulfilled, the reasons for which the Community national or company concerned wished to exercise that freedom cannot call into question the protection they derive from the Treaty"

Implementing the purposive interpretation test, AG Léger found the objectives of the freedom of establishment to require a genuine and actual pursuit of an economic activity in the host Member State in order for Treaty standing to be granted.<sup>108</sup> AG Léger stresses that the scope of the freedom of establishment is not affected by the fact that the Irish tax regime has been

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<sup>106</sup> See chapter 3 in this paper.

<sup>107</sup> *Cadbury Schweppes, PLC v. Inland Revenue*, AG's Opinion, para. 43.

<sup>108</sup> *Idem*, para. 42, 49.

blacklisted by the 'Code of Conduct' group report<sup>109</sup> or the fact that it may be classified as State aid.<sup>110</sup> This analysis leads AG Léger to the conclusion that in the instant case Treaty standing should be granted.

After confirming that the UK's CFC regime hinders the freedom of establishment, AG Léger moves to consider whether that restriction can be justified. Referring to the Court's case law, AG Léger recalls that counteracting tax avoidance is among the overriding reasons in the public interest which can justify a restriction of the fundamental freedoms.<sup>111</sup> It is in that point that the AG is offering a novelty, according to which this justification is in fact an expression of the abuse of law principle, claiming:<sup>112</sup>

"However, according to a phrase habitually used in the case-law, a hindrance to a freedom guaranteed by the Treaty can only be justified on the ground of counteraction of tax avoidance if the legislation in question is specifically designed to exclude from a tax advantage wholly artificial arrangements aimed at circumventing national law.

*The use of that formula, the language of which reproduces that of the doctrine of 'abuse of rights', may be understood as intended to prevent the counteraction of tax avoidance from being used as a pretext for protectionism. Application of Community law may be refused only when the company in question relies on it abusively because it has set up an artificial arrangement in order to avoid tax.*

...

the national courts may, case by case and on the basis of objective evidence, take account of *abuse* or fraudulent conduct on the part of the persons concerned in order to deny them the benefit of the provisions of Community law on which they seek to rely."

Interestingly, the AG, referring to the *Marks & Spencer* case, explains that the Court justified the UK's group relief there because "the freedoms introduced by the Treaty are not designed to enable companies to transfer their profits or losses from one Member State to another to suit their convenience",<sup>113</sup> thus, in fact, considering the Court's decision to be an expression of the abuse of law principle and not a justification based on the need to prevent tax avoidance. In other words, the AG is of the opinion that *Marks & Spencer* was lacking Treaty standing rather than being deprived of its right due to overriding public interest requirements.

The AG concludes that the freedom of establishment does not preclude national tax legislation of the sort of the UK's CFC regime, if that legislation applies only to prevent situations of abuse of EU law.

The Court, starts its analyses with the abuse of law question. But the analysis it offers is very thin and limits itself to the following declaration:<sup>114</sup>

"the fact that a Community national, whether a natural or a legal person, sought to profit from tax advantages in force in a Member State other than his State of residence cannot in itself deprive him of the right to rely on the provisions of the Treaty"

The Court, in its analysis of the abuse of law principle, refrains from properly implementing the purposive interpretation with regard to the freedom of establishment. This omission seems to be intentional. As will be presented shortly, the Court adopts the AG's view that the 'wholly

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<sup>109</sup> *Idem*, para. 52-53.

<sup>110</sup> *Idem*, para. 58.

<sup>111</sup> *Idem*, para. 86.

<sup>112</sup> *Idem*, para. 87-88, 91.

<sup>113</sup> *Idem*, para. 102.

<sup>114</sup> *Cadbury Schweppes, PLC v. Inland Revenue*, para. 36.

artificial arrangement' component in the tax avoidance justification duplicates the two prong test of the abuse of law principle. Therefore, if the Court would have properly implementing the purposive interpretation when examining the presence of abusive behavior, an identical analysis would have been used for the *a priori* Treaty standing analysis and the *a posteriori* justification analysis. This would have made the abolition of the prevention of tax avoidance justification very obvious. In the writer of this paper opinion, by miss-implementing the abuse of law principle the Court tried to conceal this abolition, in order to curtail Member States dissatisfaction from the ensuing narrowing down of their tax sovereignty.

After confirming that the UK's CFC regime hinders the freedom of establishment, the Court moves on to consider whether that hindrance can be justified.<sup>115</sup> The Court reiterates its rulings, that a national measure restricting the freedom of establishment may be justified where it specifically relates to 'wholly artificial arrangements' aimed at circumventing the application of the legislation of the Member State concerned.<sup>116</sup> The Court, following the AG's approach, interprets the notion 'wholly artificial arrangement' as implementing the two prong test used in the abuse of law principle, by stating:<sup>117</sup>

"As stated by the applicants in the main proceedings and by the Belgian Government and the Commission, the fact that none of the exceptions provided for by the legislation on CFCs applies and that the intention to obtain tax relief prompted the incorporation of the CFC and the conclusion of the transactions between the latter and the resident company does not suffice to conclude that there is a *wholly artificial arrangement intended solely to escape that tax*.

*In order to find that there is such an arrangement there must be, in addition to a subjective element consisting in the intention to obtain a tax advantage, objective circumstances showing that, despite formal observance of the conditions laid down by Community law, the objective pursued by freedom of establishment, as set out in paragraphs 54 and 55 of this judgment, has not been achieved"*

A purposive interpretation of the concept 'establishment' leads the Court to the conclude that the freedom of establishment protects only actual establishment in the host Member State, and the pursuit of genuine economic activity there, as oppose to a 'letter box' presence.<sup>118</sup> The Court left the final decision about the compatibility UK's CFC regime with the objectives of the freedom of establishment to the national court, which should in its ruling take account of the guidance provided.<sup>119</sup>

By implementing the two prongs test, used to examine the presence of abuse of EU law, in order to examine the existence of the prevention of tax avoidance justification, the Court in effect emptied the justification of any real substance. Any abusive behavior, according to the two prongs test, will *a priori* fall outside the scope of the Treaty freedoms, hence will not be granted Treaty standing. Therefore, any hindrance to a behavior that was granted Treaty standing could never be *a postreiori* justified by the prevention of tax avoidance justification, as the justification analysis uses the same test as the abuse analysis. The only way for a behavior to be justified according to this justification is if the Court miss-implement the Treaty standing examination, but then as well the tax avoidance justification will not be more than an expression of the abuse of law principle. This leads me to the conclusion that in

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<sup>115</sup> *Idem*, para. 46-47.

<sup>116</sup> *Idem*, para. 51.

<sup>117</sup> *Idem*, para. 63-64.

<sup>118</sup> *Idem*, para. 54, 64-68.

<sup>119</sup> Faulhaber, 22.

*Cadbury Schweppes* the Court in effect abolished the prevention of tax avoidance justification.

The basic illogic in the *Cadbury Schweppes* ruling led scholars to offer another explanation to the Court analysis. According to this explanation, the two prong test used to examine abusive behavior is not the same one used to examine the presence of 'wholly artificial arrangement'. When implemented in the ambit of the abuse of law principle the test relates to the "prohibition of abuse of EU law", but when implemented with regard to the prevention of tax avoidance justification it has a larger scope and relates generally to "prohibition of abuse of law". This means that a national anti-avoidance measure may be justified if it is aimed at preventing any abuse of law, including the Member State's tax law, and not only abuse of EU law. According to this approach, in implementing the two prongs test in the justification analysis the Court aimed to initiate a process of harmonizing the concept of abuse of law. In other words, The Court wants Member States to use the same concept of abuse of law for all cross-border situations within the internal market, even if the right being exercised is not granted by EU law.<sup>120</sup>

In the opinion of the writer of this paper this approach seems to go against the simple meaning of the Court's judgment. Admittedly, in *Cadbury Schweppes* the Court did not speak specifically on the prohibition of abuse of EU law when referring to the two prong test. But the fact that the analysis was undertaken with regard to the freedom of establishment indicates that the reference to abuse should be understood in the context of EU law.

The above-mentioned interpretation is also problematic since the cause it relates to the Court goes beyond the Court's authority. On the other hand, the analysis of the Court's judgment as presented by the writer of this paper seems to fit better with the Court's general approach, as expressed in the *Eurowings* case,<sup>121</sup> which does not perceive Member State's tax base protection as justifying hindrance to the Treaty freedoms.

But it seems that the most persuasive argument to support the claim that the prevention of tax avoidance justification does not exist independently anymore in the Court jurisprudence, but rather as an manifestation of the prohibition of abuse of EU law, can be deduced from the Court rulings after *Cadbury Schweppes*. This shall be reviewed hereinafter.

## **5.2 The Tax Avoidance Justification After *Cadbury Schweppes***

*Thin Cap Group Litigation*<sup>122</sup> involved several test cases concerning the compatibility of the UK's thin capitalization rules with the freedom of establishment. The Court did not perform an examination to identify the presence of abusive behavior, and assumed Treaty standing. Considering that a restriction on the freedom of establishment was caused, the Court went on to examine whether the "fight against abusive practices" could serve as potential justification for that restriction.<sup>123</sup> In that regard, referring to the *Cadbury Schweppes* case the Court noted:<sup>124</sup>

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<sup>120</sup> De La Feria, 429-430.

<sup>121</sup> Case C-294/97 *Eurowings Luftverkehrs AG v. Finanzamt Dortmund-Unna* [1999] ECR I-7447.

In paras 42-43 the Court stated in that regard:

"any tax advantage resulting for providers of services from the low taxation to which they are subject in the Member State in which they are established cannot be used to justify less favourable treatment in tax matters given to recipients of services established in the latter State ... such compensatory tax arrangements prejudice the very foundations of the single market".

<sup>122</sup> Case C-524/04 *Test Claimants in the Thin Cap Group Litigation v. Commissioners of Inland Revenue* [2007] ECR I-2107.

<sup>123</sup> *Idem*, para. 71.

<sup>124</sup> *Idem*, para. 75.



"In order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements *which do not reflect economic reality, with a view to escaping the tax normally due* on the profits generated by activities carried out on national territory."

Ultimately, the Court concluded that the UK's legislation would not be considered proportionate, and thus not compatible with the freedom of establishment, unless:

"that legislation provides for a consideration of objective and verifiable elements which make it possible to identify the existence of *a purely artificial arrangement, entered into for tax reasons alone*, and allows taxpayers to produce, if appropriate and without being subject to undue administrative constraints, evidence as to the commercial justification for the transaction in question"

A careful reading of the Court's judgment reviles the implementation of the prohibition of abuse of EU law two prong test in the justification analysis. The purposive interpretation is manifested in the words "*which do not reflect economic reality*", which is this test implementation with regard to the freedom of establishment, and the motive test is expressed in the words "*with a view to escaping the tax normally*". This confirms that *Thin Cap Group Litigation* follows the footsteps of *Cadbury Schweppes*.

Case *Oy AA*<sup>125</sup> concerned a Finnish tax law provision which allowed companies to deduct financial transfers within the same group of companies, provided that the companies involved were established in Finland. *Oy AA*, which is established in Finland, request that a financial transfer it made to its parent company, which was established in the UK, be recognized as deductible under the abovementioned law. The request was denied by the Finnish tax authorities and *Oy AA* appealed the decision, claiming the restriction of the tax relief to companies established in Finland hinders the freedom of establishment.

The COJ concluded that, despite the fact that the Finnish tax law caused a restriction to the freedom of establishment, it is justified due to the need to safeguard the balanced allocation of the power to impose taxes between the Member States and the need to prevent tax avoidance, taken as a whole.<sup>126</sup> The COJ reasoned that:<sup>127</sup>

"Even if the legislation at issue in the main proceedings *is not specifically designed to exclude from the tax advantage it confers purely artificial arrangements, devoid of economic reality, created with the aim of escaping the tax normally due* on the profits generated by activities carried out on national territory, such legislation may nevertheless be regarded as proportionate to the objectives pursued, taken as a whole."

The Court explained that any manner of allowing the group relief in question to apply in a cross-border situation would have the effect of allowing groups of companies to choose freely the Member State in which their profits will be taxed.<sup>128</sup>

Using the same wording as in *Thin Cap Group Litigation* to describes the 'wholly artificial arrangement' element, the Court again follows the footsteps of *Cadbury Schweppes*.

It should be noticed that a similar regime to the one dealt with in *Oy AA* was at issue in the *Marks & Spencer* case. Nevertheless, in *Marks & Spencer* the Court did not find the regime<sup>129</sup>

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<sup>125</sup> Case C-231/05 *Oy AA* [2007] ECR I-06373.

<sup>126</sup> *Idem*, para. 60.

<sup>127</sup> *Idem*, para. 63.

<sup>128</sup> *Idem*, para. 64-65.

"not specifically designed to exclude from the tax advantage it confers purely artificial arrangements", as it implied in *Oy AA*. This indicates the narrowing down of the scope of the 'wholly artificial arrangement' element after *Cadbury Schweppes*

The *Lammers*<sup>130</sup> case, which then followed, concerned a Belgian anti-avoidance legislation which provided the reclassification of interest payments, paid by a Belgian subsidiary to its parent company established in another States, as taxable dividends, if these interest payments exceeded a specific threshold.

The Court - consistently with its previous rulings – regarded this differential treatment as creating a restriction to the freedom of establishment. When examining the presence of justification the Court noticed:<sup>131</sup>

"In order for a restriction on the freedom of establishment to be justified on the ground of prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements *which do not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on national territory*"

This statement confirms once again that in the COJ case law the 'wholly artificial arrangements' doctrine coincides with the prohibition of abuse of EU law.<sup>132</sup>

*Aberdeen Property Fininvest Alpha Oy*<sup>133</sup> demonstrated this fact even in a clearer manner. The case concerned a Finnish withholding tax which was expected to be levied on dividends distribution from Aberdeen, a company governed by Finish law, to its parent, which was governed by Luxemburg law. Such withholding tax would have not been charged on distribution in a wholly internal situation.

The Court, after affirming that such legislation constitutes a restriction on the freedom of establishment,<sup>134</sup> moved to examine the justifications raised by the Finish government. Among these justifications was the need to prevent tax avoidance. The risk of tax avoidance was present because the Luxemburg parent company was not subject to tax in its State of residence.<sup>135</sup> The Court, rejecting the presence of such justification, noticed:<sup>136</sup>

"As regards, first, the argument concerning the prevention of tax avoidance, it must be recalled that, according to established case-law, a national measure restricting freedom of establishment may be justified where it specifically targets wholly artificial arrangements designed to circumvent the legislation of the Member State concerned.

*For a restriction of freedom of establishment to be justified on grounds of the prevention of abusive practices, the specific objective of such a restriction must be to prevent conduct involving the creation of wholly artificial arrangements which do not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on national territory.*"

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<sup>129</sup> *Marks & Spencer*, para. 55-57. The Court subjected the justification of the group relief regime to the fulfillment of two conditions. See chapter 3.2 in this paper.

<sup>130</sup> Case C-105/07 *Lammer & Van Cleeffs* [2008] ECR I-173.

<sup>131</sup> *Idem*, para. 28.

<sup>132</sup> L. Cerioni, "The "Abuse of Right" In EU Company Law and EU Tax Law: A Re-Reading of the COJ Case-Law and Quest for a Unitary Notion" (2010): 1-28, 13.

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<sup>133</sup> Case C-303/07 *Aberdeen Property Fininvest Alpha Oy* [2009] ECR I-0000.

<sup>134</sup> *Idem*, para. 56.

<sup>135</sup> *Idem*, para. 58.

<sup>136</sup> *Idem*, para. 63-65.

The prevention of tax avoidance justification had arguably a small scale revival in the judgment rendered in the recent *Société de Gestion Industrielle (SGI)*<sup>137</sup> case. The case concerned the Belgian transfer pricing legislation, which applied only in cross-border situations, as opposed to wholly internal situations.

The Court, after confirming the presence of a restriction on the freedom of establishment,<sup>138</sup> moved to consider whether the legislation can be justified. It concluded that in light of the need to maintain a balanced allocation of the power to tax between the Member States and to prevent tax avoidance, taken together, it must be held that such legislation is justified<sup>139</sup> as long as two conditions are fulfilled:<sup>140</sup>

- On each occasion on which there is a suspicion that a transaction goes beyond what the companies concerned would have agreed under fully competitive conditions, the taxpayer is given an opportunity, without being subject to undue administrative constraints, to provide evidence of any commercial justification that there may have been for that transaction.
- Where the consideration of such elements leads to the conclusion that the transaction in question goes beyond what the companies concerned would have agreed under fully competitive conditions, the corrective tax measure must be confined to the part which exceeds what would have been agreed if the companies did not have a relationship of interdependence.

Of special interest in this judgment is the Court's analysis with regard prevention of tax avoidance justification. In that regard the Court noted:<sup>141</sup>

"as regards the prevention of tax avoidance, it should be recalled that a national measure restricting freedom of establishment may be justified where it specifically targets wholly artificial arrangements designed to circumvent the legislation of the Member State concerned.

In that context, national legislation which is *not* specifically designed to exclude from the tax advantage it confers such purely artificial arrangements – devoid of economic reality, created with the aim of escaping the tax normally due on the profits generated by activities carried out on national territory – *may nevertheless be regarded as justified by the objective of preventing tax avoidance, taken together with that of preserving the balanced allocation of the power to impose taxes between the Member States.*"

There is no novelty in the Court's analysis of the 'wholly artificial arrangement' element, which again follows the footsteps of *Cadbury Schweppes*. Nevertheless, the Court's broadening of the tax avoidance prevention justification beyond the borders of the 'wholly artificial arrangement' doctrine, even though following the footsteps of the *Oy AA* judgment, could be claimed to announce a new dawn to this justification. In the opinion of the writer of this paper that is not the case. The fact that the Court restricted the application of such broadening only to situations where the need to preserve a balanced allocation of power to impose taxes is also at hand, implies that it will only have effect in situations that would have been justified anyway by the latter justification, which is not burdened by the 'wholly artificial arrangement' doctrine. Therefore, the tax avoidance prevention justification seems to remain a dead letter.

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<sup>137</sup> Case C-311/08 *Société de Gestion Industrielle (SGI) v. État belge* [2010] ECR-0000.

<sup>138</sup> *Idem*, para. 55.

<sup>139</sup> *Idem*, para. 69.

<sup>140</sup> *Idem*, para. 70-72.

<sup>141</sup> *Idem*, para. 65-66.

## 7. CONCLUSION

From the investigation performed in this paper, it seems that the research hypothesis was confirmed. The prevention of Member State's tax avoidance, despite being repeatedly mentioned in the Court's discourse as a justification ground for Treaty freedoms hindrance, *de facto* cannot independently justify anti tax avoidance measures. This is due to the fact that the Court has been continuously narrowing down this justification, a trend that culminated in the *Cadbury Schweppes* case where the Court restricted the application of this justification to anti avoidance measures aimed to prevent only the abuse of EU law. As the general principle prohibiting abuse of EU law *a priori* restricts abusive behaviors from being granted Treaty standing, no situation in which Treaty standing has been granted could be in effect justified by this overriding public interest. This indicates the practical abolition of the prevention of tax avoidance justification.

The alleged revival of this justification in the ambit of the recent *Société de Gestion Industrielle (SGI)* seems not to change the above conclusion, as the Court reasoning in that case clearly indicates that it can only be used as a not required auxiliary justification.

Apparently, the Court chose to conceal the abolition of the prevention of tax avoidance justification in order to prevent criticism from the Member States, the tax base of which cannot be usefully protected anymore from avoidance. But in doing so, the Court undermined the legal certainty in the EU, which is the cause of obstacles to the economic life in the Common Market.

It should be indicated that as a counter reaction to the abolition of the prevention of tax avoidance justification Member States have initiated a coordination measure with regard to some of their anti-avoidance measures (CFC and thin capitalisation rules).<sup>142</sup> It would be interesting to see if such coordination measures will replace the abolished justification in other cases in the future.

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<sup>142</sup> See chapter 2.2 in this paper.

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