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EURO TAX FLASH
KPMG'S EU TAX CENTRE

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CJEU decision in the Groupe Steria case

Freedom of establishment – Parent-Subsidiary Directive – Group taxation – 5% non-deductible charges - balanced allocation of taxing rights - coherence

On September 2, 2015, the Court of Justice of the European Union (CJEU) ruled that the French rules that allow a French parent company a full exemption in respect of dividends received from domestic subsidiaries under a group taxation regime, but effectively tax (up to) 5% of dividends received from shareholdings in EU subsidiaries, are in breach of the freedom of establishment.

Background

Under the French participation exemption regime, dividends distributed by a subsidiary to a parent company are, in principle, tax exempt at the level of the parent company, with the exception of a fixed amount of 5% representing the charges incurred in relation to the holding in the subsidiary. However, the French group taxation regime allows the deduction of this fixed 5% add-back if both the parent company and the subsidiary are jointly taxed and part of a single tax group.

The Administrative Court of Appeal of Versailles referred the question whether the French rules infringed the EU freedom of establishment to the CJEU.

CJEU Decision

According to the CJEU, a French parent with a non-French subsidiary is treated less favorably than a French parent with a French subsidiary, since it is only possible for a French parent company to receive 100% tax-exempt dividends in the case of holdings in domestic companies belonging to the same tax group. By contrast, profits distributed by non-resident companies, under the same conditions, are only 95% tax-exempt. This is due to the fact that the group taxation regime is not open to the foreign subsidiaries, thereby effectively disallowing the French parent from claiming the benefit of the deduction of the 5% add-back. Referring to its earlier case law, the CJEU also noted that French subsidiaries forming part of a tax group with a French parent company are in a comparable situation to foreign subsidiaries. As a consequence, this difference in treatment constitutes a restriction to the freedom of establishment.

The CJEU further considered, but rejected, a number of possible justifications. Referring to the opinion issued by Advocate General Kokott, the Court concluded that, unlike the X-Holding case (C-337/08), no justification can be found in the preservation of the allocation of taxing powers between Member States, since the disputed provision relates to charges incurred solely by the French parent company and no other fiscal jurisdiction is involved. Second, the Court analyzed whether the different treatment can be justified on the basis of the coherence of the French tax system. In that case there must be a direct link between the disputed tax advantage and a corresponding tax levy. Since there is no corresponding tax disadvantage, as opposed to the facts at issue in the Papillon case (C-418/07), the Court concluded that this justification also does not apply. Finally, the Court dismissed the argument that the Parent-Subsidiary Directive allows Member States to deny the deduction of any charges up to 5% of the dividends distributed by a foreign subsidiary and relating to the holding of the latter. Indeed, it is established case law that such a prohibition may only be applied in a manner that is not contrary to the fundamental freedoms.

EU Tax Centre Comment

The CJEU's decision is largely based on its previous case law and to that extent was generally anticipated.

The French Tax Authorities and French Courts must now settle the pending cases. It is likely that French law will be amended to take account of the CJEU decision and this could result in the benefit of being able to deduct the 5% add-back being withdrawn in respect of French dividends.

Should you require further assistance in this matter, please contact the EU Tax Centre or, as appropriate, your local KPMG tax advisor.

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