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ATOZ ALERT

The modification of a vertical tax consolidation group into a horizontal tax consolidation group does not end the tax consolidation regime

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On 14 May 2020, the Court of Justice of the European Union ("CJEU") ruled on the Luxembourg tax consolidation regime and took a very positive decision for the Luxembourg corporate taxpayers. In its ruling, the CJEU rejects the interpretation and the application of the Luxembourg tax consolidation regime made by the tax authorities.

The position taken by the CJEU is in line with the arguments we developed extensively in an article published in the Revue de Droit Fiscal entitled "L'intégration fiscale : besoin de clarifications suite aux évolutions et controverses récentes" and in our ATOZ Insights dated February 2019.

Background

Since 2015, the Luxembourg tax consolidation regime makes the distinction between the vertical consolidation where the results are consolidated at the level of an integrating parent company and the horizontal tax consolidation where the tax results are consolidated at the level of an integrating subsidiary company.

Horizontal tax consolidation was introduced in 2015 following a CJEU ruling. On 12 June 2014, the CJEU concluded that not allowing a tax consolidation between two Dutch sister subsidiaries, on the ground that the parent company was not resident in the Netherlands, was not compliant with EU law. Despite the fact that horizontal tax consolidation was not possible at all in Luxembourg, the Luxembourg legislator decided to amend its tax consolidation regime to echo the European case law.

Based on the 2014 CJEU case law, and in anticipation of the introduction of the horizontal tax consolidation regime in Luxembourg tax law, some Luxembourg companies requested the application of such a regime retroactively as from 2013. This was the case of two Luxembourg companies (LuxCo B and LuxCo C) which requested to be integrated into an existing tax consolidation group, meaning that they requested to be horizontally integrated with their sister company LuxCo A, the integrating company of an existing vertical tax consolidation (LuxCo A remaining the integrating entity of the tax consolidation which would have become horizontal).

The benefit of such a regime was however denied by the tax authorities and the taxpayers lodged appeals against the tax authorities' position. As a result, on 29 November 2018, the Luxembourg Administrative Court raised prejudicial questions to the CJEU. On 14 May 2020, the CJEU ruled on the Luxembourg tax consolidation regime.

Position of the CJEU

- ***EU compliance of the "old" tax consolidation regime***

On the question whether the previous Luxembourg tax consolidation regime (prior to being amended in 2015) was in line with EU law (in other words, was a regime which did not allow the horizontal tax consolidation EU-compliant or not), unsurprisingly, the CJEU decided that it was contrary to the EU law.

According to the CJEU, the freedom of establishment must be interpreted as prohibiting the legislation of a Member State which, while allowing vertical tax integration between a resident parent company or a permanent establishment in that Member State of a non-resident parent company, and its resident subsidiaries, does not allow horizontal tax integration between the resident subsidiaries of a non-resident parent company.

This part of the CJEU's decision should have a quite relative effect for the Luxembourg companies, in the future, as the Luxembourg legislator already amended the tax consolidation regime introducing the horizontal tax consolidation.

- ***Requirement to end the vertical consolidation (with a potential retroactive effect if the 5-year period is not met) in order to benefit from the horizontal tax consolidation***

According to the Luxembourg case law, any modification to a tax consolidation group at the level of the integrated companies does not put an end to the group and the creation of a new group. However, on the basis that the Luxembourg tax law does not allow a company to simultaneously be part of more than one tax consolidated group, the Luxembourg tax authorities require, in case a vertical tax consolidation group is modified by adding sister companies of the integrating company (and thus the change of tax consolidation regime from vertical to horizontal), to end the vertical tax consolidation (with the consequence that the computation of the 5-year period is interrupted) in order to benefit from the horizontal tax consolidation.

The Luxembourg Administrative Court asks to the CJEU whether the strict separation of vertical and horizontal tax consolidation is in line with EU law. In other words, is it EU-compliant to be required to end the vertical tax consolidation before being able to benefit from a horizontal tax consolidation?

In this respect, the CJEU decides that the freedom of establishment should be interpreted as prohibiting a legislation of a Member State which has the effect to force a parent company having its seat in another Member State to dissolve an existing vertical tax integration between one of its subsidiaries and a certain number of its resident sub-subsidiaries in order to allow this subsidiary to proceed with a horizontal tax integration with other resident subsidiaries of the said parent company, when the resident integrating subsidiary remains the same and the dissolution of the vertical tax integration before the end of the minimum period of integration, provided for by national law, implies the tax reassessment of the companies concerned, on an individual basis.

This decision is very positive for the Luxembourg taxpayer as it puts an end to the restrictive interpretation and application of the Luxembourg tax consolidation regime applied by the tax authorities. As long as the integrating company remains the same and that all the other legal conditions are met, an existing tax consolidation group can now be extended to additional subsidiaries or sub-subsidiaries of the integrating company but also to a sister company of such integrating company, which was denied by the tax authorities.

- ***Timing for requesting the application of the horizontal tax consolidation***

In Luxembourg, tax consolidation is only available upon filing a written request with the Luxembourg tax authorities, filed by the integrating company, the integrated entities subject to the tax consolidation as well as by the non-integrating parent company in case of horizontal tax consolidation. Tax consolidation is effective retrospectively as of the beginning of the fiscal year during which the tax consolidation was requested. As a result, to benefit from the tax consolidation regime as from 1.1.2013, you have to request its application by 31.12.2013 at the latest.

The last question raised by the Administrative Court to the CJEU was whether, in case the tax consolidation regime was to be considered as not compliant with EU law by the CJEU, the requirement that the tax consolidation request had to be filed before the end of the first tax year in respect of which tax consolidation was applied for is in line with EU law to the extent that it precludes companies to benefit from the lesson learned from the CJEU rulings on the Dutch tax consolidation regime in 2014. So, in other words, is it compliant with EU law to require the tax consolidation request to be filed before the end of the first tax consolidation year in respect of tax years preceding the CJEU decision?

According to the CJEU, the principles of equivalence and effectiveness must be interpreted as meaning that they do not preclude a law of a Member State relating to a system of tax consolidation which provides that any request to benefit from such a regime must be submitted to the competent authority before the end of the first tax year for which the application of this regime is requested.

As a result, a taxpayer cannot request retroactively the application of the tax consolidation regime based on a CJEU ruling. However, a taxpayer can submit a request to benefit from the tax regime as detailed in the CJEU ruling as from the tax year of the publication of the latter or, if a tax consolidation request was submitted for a previous tax year, but denied by the tax authorities on the basis of the restrictive interpretation of the Luxembourg tax consolidation regime, the taxpayer should in principle be allowed to challenge such denial on the basis of the CJEU decision.

Luxembourg taxpayers having a tax consolidation group or who have submitted a request to modify their tax consolidation, but that such a request has been denied, should seek advice from their tax adviser in order to analyse the potential impact of this case law on their structure.

Do you have further questions?

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