Tax Alert

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# Dividends received from 95% EU subsidiaries : CJEU rules French tax consolidation regime infringes EU law

In an awaited decision issued on 2 September 2015 (case C-386/14), the Court of Justice of the European Union (CJEU) concludes that the difference in taxation of dividends received by French parent companies of a tax consolidated group depending on whether the subsidiaries are established in France or the EU, is contrary to the freedom of establishment. The CJEU decision follows the opinion issued by Advocate General Kokott on 11 June 2015.

## Background on the case

Under French tax law, when a French parent company receives dividends from a subsidiary, the dividends are 95% tax exempt under the domestic participation exemption regime (provided certain requirements are met). The remaining 5% is deemed to represent nondeductible costs and is taxed at the standard corporate income tax rate. The 95% participation exemption regime applies regardless of whether dividends are received from a French subsidiary or a subsidiary in another state (whether within or outside the EU, except for non cooperative states). However, under a special rule of the French tax code, the 5% deemed expenses may be deducted from profits if a French parent company and its French 95% held subsidiaries are members of the same tax consolidation group, with the result that a full exemption can be obtained in such a case. However, a company that is not resident in France cannot join a French tax consolidated group, so a cross-border arrangement cannot benefit from the 100% exemption.

Steria, the head of a French tax group, was denied the deduction of the 5% proportion for costs and expenses in respect of revenue that one of its French subsidiaries received from holdings in companies established in other EU member states. Steria did in fact accept the exclusion of these foreign companies from the tax group but took the view that the French legislation was inconsistent with the freedom of establishment insofar as it does not allow the full exemption of dividends received from an EU subsidiary that cannot be part of the French group because of its residence abroad.

The Administrative Court of Appeal of Versailles referred the case to the CJEU on 13 August 2014 for a preliminary ruling.

## CJEU decision

The CJEU rules that the freedom of establishment is restricted as the treatment of a parent company, member of a tax group, that has domestic subsidiaries is more advantageous than the one of a parent company with subsidiaries in other Member States. The French legislation makes it therefore less attractive for those companies to exercise their freedom of establishment, as they would be deterred from setting up subsidiaries in other Member States. The Court also ruled that such a difference of treatment cannot be justified by the need to safeguard the balanced allocation of the power to impose taxes between the Member States, or by the need to safeguard the cohesion of the French tax system.

It concludes that the freedom of establishment precludes rules of a Member State that govern a tax integration regime under which a tax integrated parent company is entitled to neutralization as regards the add-back of a propor-

tion of costs and expenses, fixed at 5% of the net amount of the dividends received by it from tax-integrated resident companies, whereas those rules prevent such neutralization for dividends from subsidiaries located in another Member State, which, had they been resident, would have been eligible in practice, if they so elected.

## Comments

Affected groups may be entitled to obtain a refund of corporate income tax paid on the taxable 5% portion of dividends received form subsidiaries resident in other member states, provided certain conditions are satisfied.

They, therefore, should consider filing protective claims to preserve their rights to restitution for fiscal years 2012, 2013 and 2014 (no later than 31 December 2015 for corporate income tax paid in 2013) from being barred by the statute of limitations.

The French Ministry of Finance has not yet announced whether or to which extent the French tax group regime will be amended (by the next Finance laws). It could be decided to put an end to the provisions allowing the full exemption mechanism under French consolidation group regime.

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