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Full expense deduction for tax group members also for foreign subsidiaries

The ECJ has held that provisions allowing full expense deduction within tax groups must be applied to otherwise eligible foreign subsidiaries.

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In France, dividends are exempt in the hands of a corporation holding at least 5% of the shares in the payer. However, 5% of the exempt amount is disallowed as a deduction to reflect the business expenses deemed directly attributable. A parent may opt to pool its results with those of some or all of its domestic subsidiaries in which it holds directly or indirectly at least 95%. The effect of this pooling is to tax the income of the subsidiaries only once, although there is no corresponding 5% expense disallowance. Group members are thus privileged over otherwise qualifying subsidiaries remaining outside. Since foreign subsidiaries are excluded *per se* from French tax groups, they are excluded from the privilege. The ECJ has now held that this exclusion is an unwarranted restriction on the parent company's freedom of establishment in other member states.

The ECJ continues to accept the exclusion of foreign subsidiaries from tax groups as such as being necessary to preserve the agreed allocation of taxing rights between member states. However, it does not accept the consequence of an unavoidable expense disallowance on the profits received from subsidiaries otherwise qualifying for tax group membership merely because of their foreign residence. This discrimination is a unilateral measure which cannot be justified on the basis of different circumstances, by the need to protect the cohesion of the tax system or by reference to an offsetting disadvantage.

The consequences of this ruling for other countries remain to be seen. Ultimately they will depend on the degree to which local law regards the situation of group members as comparable to that of non-members. In Germany, members of a tax group must sign a court-registered profit pooling agreement to run for at least five years. This requirement to actually surrender the profits might be seen as placing a group subsidiary in a different position from a subsidiary outside the group. On the other hand the qualifying shareholding for group membership is a simple majority of the voting rights. This is a less stringent requirement than that in force in France.

The ECJ case reference is C-386/14 *Groupe Steria* judgment of September 2, 2015.

Schlagwörter

foreign subsidiaries, tax group