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Swedish interest deduction rule incompatible with EU law

In a recent judgement the European Court of Justice (ECJ) has clarified that it is contrary to the freedom of establishment to deny the deduction of interest costs on a loan from a normally taxed group company, if this would not have happened had the loan been granted from a normally taxed Swedish group company instead.

The case was brought forward by the Supreme Administrative Court in Sweden and shows that a deduction of arm's length cross-border intra-group interest can hardly be restricted with regard to the EU fundamental freedoms, even if the motive of the loan is to obtain a significant tax advantage.

A brief overview:

Lexel is a Swedish company and part of the Schneider Electric group. The group's parent company is Schneider Electric SE (France). In December 2011, Lexel acquired the 15% of the shares in Schneider Electric Services International Belgium SPRL (SESI) which formerly was owned by SEE (a group company established in Spain), by taking out a loan from Bossière Finances SNC (BF), an internal bank of the Schneider Electric group. - Lexel, BF, SESI and SEE are all, directly or indirectly, subsidiaries of Schneider Electric Industries.

According to the Swedish tax administration, which refused to allow the deduction of the interest charges on the loan granted by BF, the transactions were carried out to deduct the interest costs related to the acquisition of the shares in SESI in Sweden rather than in Spain and thus resulting in a substantial tax benefit. It is important to add that a deduction of the interest expenses connected with that loan could have been deductible if BF had been established in Sweden.

The ECJ therefore held that there is a difference in treatment which is not in line with the fundamental freedom of establishment in Article 49 TFEU. Such a difference in treatment may, however, be compatible with Article 49 TFEU if it relates to circumstances (situations) which are not objectively comparable or if it is justified by an overriding reason in the public interest and is proportionate to that objective. The ECJ held that, foremost, there was **no comparability,** since a situation in which a company established in one Member State makes interest payments on a loan taken out from a company established in another Member State and belonging to the same group is no different from a situation in which the recipient of the interest payments is a company belonging to the group and established in the same Member State, namely Sweden. Also, the **difference in treatment is not justified by overriding reasons** in the public interest. Specifically, the ECJ saw no justification based on the need to preserve the balanced allocation of the power to impose taxes between the Member States and the fight against tax avoidance.

For an **in-depth analysis of the ECJ judgement** we recommend our **EU Direct Tax Newsalert** of 21 January 2021.

Schlagwörter

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