

Dual Residence and Directive Shopping

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1. Introduction

The term “*directive shopping*” was first used by *Knobbe-Keuk* in 1992¹ and describes the situation in which a person “*shops*” into an otherwise inapplicable directive², aiming at taking advantage of the directive provisions.³ Directive shopping is, like treaty shopping, a form of tax avoidance. Thereby one operation is split into two or more operations, the economic effect of which is the same.⁴

There is for instance directive shopping in the area of the Parent-Subsidiary Directive if a company resident in a third State which expects to derive dividends from a company established in a Member State sets up a conduit company in another Member State that will receive the dividends tax exempt under the directive and channels them according to a more favorable double taxation convention between the intermediate Member State and the third State without or with reduced withholding taxes to the ultimate shareholder outside the Community.⁵

There could also be directive shopping solely within the Community if a parent company of a Member State plans to own a shareholding in a company resident in another Member State, the dividends of which would not qualify for the participation exemption in the parent Member State. Therefore, a wholly owned subsidiary in a third Member State could be interposed to hold the shares under more favorable conditions according to which the participation exemption applies; it would then channel the dividends tax exempt into the parent company’s Member State, which applies its participation exemption in relation to the wholly owned intermediate company since the required participation threshold imposed by the directive is satisfied.⁶

For making such schemes work the requirements for qualifying companies under the respective directive, as further implemented by the national legislation of the Member States involved, must be met. Moreover, those structures face general and specific anti-abuse provisions. The following contribution focuses on directive shopping aspects

¹ Knobbe-Keuk, “The EC Corporate Tax Directives – Anti-Abuse Provisions, Direct Effect, German Implementation Law”, 20 *Intertax* (1992), p. 490; see De Broe, *International Tax Planning and Prevention of Abuse* (Leuven: International Bureau of Fiscal Documentation, 2008), p. 20.

² The following contribution deals with Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, OJ L 225, 22 September 1990, p. 6 (hereafter “*Parent-Subsidiary Directive*”), Council Directive 90/434/EEC of 23 July 1990 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office, of an SE or SCE, between Member States, OJ L 225, 20 August 1990, p. 1 (hereafter “*Merger Directive*”) and Council Directive 2003/49/EC of 3 June 2003 on a common system of taxation applicable to interest and royalty payments made between associated companies of different Member States, OJ L 157, 26 June 2003, p. 49 (hereafter “*Interest and Royalty Directive*”).

³ De Broe, supra note 1, p. 23.

⁴ De Broe, supra note 1, p. 24.

⁵ De Broe, supra note 1, pp. 22–23.

⁶ De Broe, supra note 1, pp. 23–24.

of dual resident companies in the area of the direct tax directives at a Community law level apart from specific domestic implementation measures of the Member States.

2. Direct Tax Directives

2.1. Requirements for the Directive Entitlement of Dual Resident Companies

The direct tax directives apply to qualifying companies of the Member States. For the purposes of the Parent-Subsidiary Directive and the Merger Directive, a qualifying company is any company which (among other requirements) is “*according to the tax laws of a Member State [...] considered to be resident in that State for tax purposes and, under the terms of a double taxation agreement concluded with a third State, is not considered to be resident for tax purposes outside the Community*”.⁷ The Interest and Royalty Directive contains a similar provision according to which a qualifying company of a Member State is any company “*which in accordance with the tax laws of a Member State is considered to be resident in that Member State and is not, within the meaning of a Double Taxation Convention on Income concluded with a third state, considered to be resident for tax purposes outside the Community*”.⁸

For tax treaty purposes a dual resident company is usually considered to be resident outside the Community when the place of effective management lies in a third State: “*Where [...] a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident only of the State in which its place of effective management is situated*” (Art. 4(3) OECD MC). However, any other tie breaker rule is sufficient as well.^{9, 10}

In respect of the fiscal residence criteria of the directives the following relevant constellations of dual resident companies with Community nexus can be distinguished:

- Dual resident companies having both of their residences within the Community;
- dual resident companies which are resident in a third State and resident in the Community in the absence of a double taxation convention concluded between those States;
- dual resident companies which are resident in a third State and resident in the Community where there is a double taxation convention concluded between those States according to which

⁷ Art. 2(1)(b) Parent-Subsidiary Directive and Art. 3(b) Merger Directive.

⁸ Art. 3(a)(ii) Interest and Royalty Directive.

⁹ See Tumpel, “Die Bedeutung der abkommensrechtlichen Ansässigkeit für die Mutter-Tochter-Richtlinie und die Fusionsrichtlinie”, in: Gassner, Lang and Lechner (Eds.), *Doppelbesteuerungsabkommen und EU-Recht* (Vienna: Linde, 1996), p. 197.

¹⁰ See for example Art. 4(4) U.S. MC: “*Where [...] a company is a resident of both Contracting States, then if it is created or organized under the laws of one of the Contracting States [...], but not under the laws of the other Contracting State [...], such company shall be deemed to be a resident of the first-mentioned Contracting State*”.

- the Member State is deemed to be the State of residence for treaty purposes;
- the third State is deemed to be the State of residence for treaty purposes.

Only in the last sub-constellation are the requirements for the respective directive application not met *per se* since the tie being broken by a tax treaty allocates the residence for treaty purposes outside the Community (see for such situations outside the subjective scope *infra* 3.).¹¹ In all other constellations the fiscal residence criterion is met and therefore the directives, in principle, are applicable, provided that the other requirements for a company to qualify for directive purposes are satisfied.¹²

Secondary Community law is hierarchically subordinate to primary Community law, as the former is derived from the latter under Art. 249(1) EC Treaty. Accordingly, secondary Community law must comply with primary Community law, especially with the fundamental freedoms.¹³ Thus, the question arises whether the direct tax directives possibly infringe the fundamental freedoms by excluding dual resident companies *per se* if a tax treaty allocates their residence for treaty purposes outside the Community. However, directive provisions giving Member States latitude in implementation of the directive do not themselves infringe the fundamental freedoms if the margin left is sufficiently wide to transpose them into domestic law in a manner consistent with primary Community law.^{14, 15} Since the directives do not oblige Member States to implement them in a way excluding such third State dual resident companies from the same benefits under domestic tax law, the author considers them to be in line with the fundamental freedoms.¹⁶

¹¹ Terra and Wattel, *European Tax Law* (Alphen aan den Rijn: Kluwer, 5th edition 2008), p. 479.

¹² For the other requirements, see Art. 2 and 3 Parent-Subsidiary Directive, Art. 3 Merger Directive and Art. 3 Interest and Royalty Directive.

¹³ See Kofler, “The Relationship between the Fundamental Freedoms and Directives in the Area of Direct Taxation”, *DPTI* (2009), in print, with further references.

¹⁴ See Kofler, *supra* note 13, in print, with further references.

¹⁵ If a directive permits certain domestic measures under its scope, those measures may nevertheless only be exercised in compliance with primary Community law; see ECJ, 18 September 2003, Case C-168/01 *Bosal* [2003] ECR-9409, para. 26: “However, that possibility may be exercised only in compliance with the fundamental provisions of the Treaty”; ECJ, 23 February 2006, Case C-471/04 *Keller Holding* [2006] ECR-2107, para. 45; see in contrast the heavily criticized Case ECJ, 5 October 2004, C-475/01 *Commission v. Greece* (“*Ouzo*”) [2004] ECR-8923, where a directive contained explicit permission for a specific Member State; see Kofler, *supra* note 13, in print, with further references.

¹⁶ See in this context the pending ECJ Case C-247/08, *Gaz de France*, where the Finanzgericht Köln referred the following question for preliminary ruling: “*Inasmuch as Article 2(a) in conjunction with paragraph (f) of the Annex to Council Directive 90/435/EEC of 23 July 1990 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States together with Article 5(1) of the same directive in the event of a profit distribution by a German subsidiary establishes an exemption from withholding tax in favour of French parent companies taking the legal form of a 'société anonyme', 'société en commandite par actions' or 'société à responsabilité limitée' not, however, French parent companies taking the legal form of a 'société par actions simplifiée' do such provisions infringe Articles 43 EC and 48 EC or Article 56(1) EC and Article 58(1)(a) and (3) EC?*”.

2.2. General Anti-Abuse Provisions

The direct tax directives grant Member States a certain discretionary power to apply domestic or treaty-based anti-abuse provisions in derogation of the substantive directive rules.¹⁷

- According to Art. 1(2) Parent-Subsidiary Directive, the “*Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse*”.
- Art. 11(1)(a) Merger Directive provides that Member States “*may refuse to apply or withdraw the benefit[s ...] where it appears that the merger, division, partial division, transfer of assets, exchange of shares or transfer of the registered office of an SE or an SCE [...] has as its principal objective or as one of its principal objectives tax evasion or tax avoidance; the fact that one of the operations referred to in Article 1 is not carried out for valid commercial reasons such as the restructuring or rationalisation of the activities of the companies participating in the operation may constitute a presumption that the operation has tax evasion or tax avoidance as its principal objective or as one of its principal objectives*”.
- According to Art. 5 Interest and Royalty Directive, the “*Directive shall not preclude the application of domestic or agreement-based provisions required for the prevention of fraud or abuse [...] Member States may, in the case of transactions for which the principal motive or one of the principal motives is tax evasion, tax avoidance or abuse, withdraw the benefits of this Directive or refuse to apply this Directive*”.

Terra and *Wattel* expect the ECJ to take little notice of the different wordings of the general anti-abuse provisions and to apply them in the same manner.¹⁸ The anti-abuse provisions do not seem to introduce an autonomous Community concept of abuse. They merely specify that Member States may, even if the requirements for applying the directive are fulfilled rely on national and treaty based anti-abuse provisions to deny or to limit the directive benefits.¹⁹ Hence, the general anti-abuse provisions seem to be largely redundant. Directive shopping structures could be countered under the ECJ’s general “*abuse of rights*” doctrine as well.²⁰

Within the scope of the directives Member States may refuse to grant the benefits provided by the latter where it appears that an operation is not carried out for valid

¹⁷ *Terra* and *Wattel*, supra note 11, p. 508.

¹⁸ *Terra* and *Wattel*, supra note 11, p. 622.

¹⁹ *Terra* and *Wattel*, supra note 11, pp. 508–509.

²⁰ *Terra* and *Wattel*, supra note 11, p. 511, p. 557 and p. 622; regarding Art. 1(2) Parent-Subsidiary Directive, Züger, “*Mißbrauch im europäischen Unternehmensteuerrecht*”, in: Gassner and Lang (Eds.), *Besteuerung und Bilanzierung international tätiger Unternehmen* (Vienna: Orac and Linde, 1998), p. 559 et seq. and Tumpel, *Harmonisierung der direkten Unternehmensbesteuerung in der EU* (Vienna: Verlag Österreich, 1994), p. 286, in respect of fraud.

commercial reasons, but has as its essential aim the obtaining of a tax advantage.^{21, 22} Thus, purely tax-driven structures are not protected.

In the *Leur-Bloem* case the ECJ characterized the anti-abuse provision of the Merger Directive as a “*reservation of competence*” by the Member States, which must be interpreted narrowly since the general object and purpose of the directive is the taking away of tax obstacles.²³ Furthermore, the Court did not accept an automatic exclusion according to predetermined general criteria. Each particular case must be subject to a general examination with the possibility of demonstrating that a structure, although entering the scope of anti-abuse provisions, nevertheless served *bona fide* business purposes. Moreover, this examination must be open to judicial review.²⁴ These findings should be correspondingly applicable to the anti-

²¹ ECJ, 17 July 1997, Case C-28/95 *Leur-Bloem* [1997] ECR-4161, paras. 38–40; see further regarding the 6th VAT Directive ECJ, 21 February 2006, Case C-255/02 *Halifax* [2006] ECR-1751, para. 75: “[I]t must also be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage. [...] The prohibition of abuse is not relevant where the economic activity carried out may have some explanation other than the mere attainment of tax advantages”; Schön, “Rechtsmissbrauch und Europäisches Steuerrecht”, in: Kirchhof and Nieskens (Eds.), *Festschrift für Wolfram Reiß* (Cologne: Schmidt, 2008), p. 594 et seq.; Lang, “Abuse of law and Community law – In the light of *Halifax* and *Cadbury Schweppes*”, *Steuer und Wirtschaft International* (2006), p. 279; regarding the relevance of *Halifax* for direct tax directives, see Rousselle and Liebman, “The Doctrine of the Abuse of Community Law: The Sword of Damocles Hanging over the Head of EC Corporate Tax Law?”, 46 *European Taxation* 12 (2006), p. 562.

²² On the contrary, under the fundamental freedoms tax planning explicitly aimed at taking advantage of a lower tax burden is in itself not abusive; see ECJ, 12 September 2006, Case C-196/04 *Cadbury Schweppes* [2006] ECR-7995, paras. 36, 49; see further ECJ, 11 December 2003, Case C-364/01 *Barbier* [2003] ECR-15013, para. 71; ECJ, 28 January 1986, Case 270/83 *Commission v France* [1986] ECR-273, para. 21; ECJ, 26 June 2003, Case C-422/01 *Skandia and Ramstedt* [2003] ECR-6817, para. 52; ECJ, Advocate General Léger’s Opinion, 2 May 2006, Case C-196/04 *Cadbury Schweppes* [2006] ECR-7995, para. 51: “The level of taxation is a factor which a company may legitimately take into account in choosing the host State in which it intends to establish a subsidiary. A company may, without infringing the scope and spirit of Article 43 EC, decide to pursue its secondary activities in another Member State in order to benefit from the more favourable tax regime of that other State in respect of taxable activities in that State”; Vinther and Werlauff, “Tax Motives Are Legal Motives – The Borderline between the Use and Abuse of the Freedom of Establishment with Reference to the *Cadbury Schweppes* Case”, 46 *European Taxation* 8 (2006) p. 384; Schön, supra note 21, p. 582 and p. 594.

²³ Case C-28/95, *Leur-Bloem* [1997] ECR I-4161 paras. 39 and 45; Terra and Wattel, supra note 11, p. 510, p. 552 and p. 622.

²⁴ ECJ, 17 July 1997, Case C-28/95 *Leur-Bloem* [1997] ECR-4161, paras. 40–44; see further ECJ, 21 November 2002, Case C-436/00 *X and Y* [2002] ECR-10829, paras. 42–43; Hoenjet, “The *Leur-Bloem* judgment: the jurisdiction of the European Court of Justice and the interpretation of the anti-abuse clause in the Merger Directive”, 6 *EC Tax Review* (1997), p. 206 et seq.; Schön, supra note 21, p. 576; Terra and Wattel, supra note 11, p. 510, pp. 553–555 and p. 622; Panayi, Treaty Shopping and Other Tax Arbitrage Opportunities in the European Union: A Reassessment – Part 2, 46 *European Taxation* 4 (2006), p. 153.

abuse provisions of the Parent-Subsidiary Directive and the Interest and Royalty Directive.²⁵

As restrictions of Community rights, anti-abuse provisions must be applied in accordance with the proportionality principle. Therefore, the measures taken must be appropriate for combating possible abusive schemes and they may not be more restrictive than necessary for reaching that goal.²⁶

2.3. Specific Anti-Abuse Provisions regarding Dual Resident Companies

From the *Denkavit*, *VITIC* and *Voormeer* cases it can be derived that general anti-abuse provisions may not be relied on by Member States in situations where the directives already deal with in specific anti-abuse provisions (*lex specialis derogat legi generali*).²⁷ In *Denkavit*, *VITIC* and *Voormeer* the ECJ interpreted the minimum holding period requirement of Art. 3(2) Parent-Subsidiary Directive whereby Member States are entitled to exclude companies from the directive application which do not maintain their holdings for an uninterrupted period of at least two years. The Court held that this provision “*is aimed in particular at counteracting abuse whereby holdings are taken in the capital of companies for the sole purpose*

²⁵ Hoenjet, supra note 24, pp. 212–213; Schelpe, “The Denkavit-VITIC-Voormeer case”, 6 *EC Tax Review* (1997), p. 21; Terra and Wattel, supra note 11, p. 510; for the situation before the *Leur-Bloem* judgment, see Weber, “A closer look at the general anti-abuse clause in the Parent-Subsidiary Directive and the Merger-Directive”, 5 *EC Tax Review* (1996), pp. 66–67; Rädler, “Do national anti-abuse clauses distort the internal market?”, 34 *European Taxation* 9 (1994), p. 312; Farmer, “National anti-abuse clauses and distortion of the single market. Comments on Prof. Dr. Rädler’s article”, 34 *European Taxation* 9 (1994), p. 314.

²⁶ Züger, supra note 20, pp. 565–566; Terra and Wattel, supra note 11, pp. 509–510; Farmer, supra note 25, p. 314; Weber, supra note 25, pp. 67–68; ECJ, 17 July 1997, Case C-28/95 *Leur-Bloem* [1997] ECR-4161, paras. 43–44.

²⁷ ECJ, 17 October 1996, Joined Cases C-283/94, C-291/94 and C-292/94 *Denkavit*, *VITIC* and *Voormeer* [1996] ECR-5063, paras. 30–32, where Germany could not rely on Art. 1(2) in order to widen the scope of the specific anti-abuse provision of Art. 3(2): “*Secondly, the Bundesamt and the German Government submit that the interpretation applied in the transposition of Article 3(2) of the Directive by the German legislature is supported by Article 1(2) [...] It is to be noted that Article 1(2) of the Directive is a provision of principle, the content of which is explained in detail in Article 3(2) thereof. Thus, Article 3(2) and this is not disputed by any of the parties which have submitted observations to the Court is aimed in particular at counteracting abuse whereby holdings are taken in the capital of companies for the sole purpose of benefiting from the tax advantages available and which are not intended to be lasting. In those circumstances, it is not appropriate to refer to Article 1(2) of the Directive in interpreting Article 3(2). [...] So, Member States cannot make the grant of the tax advantage provided for by Article 5(1) of the Directive subject to the condition that, at the moment when profits are distributed, the parent company should have had a holding in the subsidiary during the minimum period laid down pursuant to Article 3(2), so long as this period is subsequently observed*”; Weber, “The first steps of the ECJ concerning an abuse-doctrine in the field of harmonized direct taxes”, 6 *EC Tax Review* (1997), p. 22 et seq.; Terra and Wattel, supra note 11, p. 509; Hoenjet, supra note 24, p. 212; Panayi, supra note 24, p. 153.

of benefiting from the tax advantages available and which are not intended to be lasting”²⁸.

The same must hold true for the fiscal residence criteria of Art. 2(1)(b) Parent-Subsidiary Directive, Art. 3(b) Merger Directive and Art. 3(a)(ii) Interest and Royalty Directive. As illustrated above, these provisions disqualify dual resident companies one residence of which is in a third State that is deemed to be the State of residence according to a double taxation convention. Although defining the subjective scope of the directives, the author considers the object of these provisions is in particular to counteract abusive directive shopping of third State companies.²⁹ Due to the existence of these specific anti-abuse provisions Member States may not rely on the general anti-abuse provisions of the directives in excluding companies from directive benefits in respect of their dual residence, if such companies

- are resident in two States, both of which are within the Community,³⁰
- are resident in a third State and resident in a State within the Community in the absence of a double taxation convention concluded between those States, or
- are resident in a third State and resident in a State within the Community in the existence of a double taxation convention concluded between those States according to which the Member State is deemed to be the State of residence for treaty purposes.

In other words: Within the scope of application of the direct tax directives dual residence in itself can never be an abusive structure that could be countered by Member States.

3. Dual Resident Companies outside the Subjective Scope of the Direct Tax Directives

As illustrated above, dual resident companies which are resident in a third State and resident within the Community are outside the subjective scope of the direct tax directives, if according to a double taxation convention concluded between those States the third State is deemed to be the State of residence for treaty purposes.³¹ Such third State dual resident companies were probably excluded from

²⁸ ECJ, 17 October 1996, Joined Cases C-283/94, C-291/94 and C-292/94 *Denkavit, VITIC and Voormeer* [1996] ECR-5063, para. 31; see also for the characterization as anti-abuse provision, Terra and Wattel, *supra* note 11, p. 484; Weber, *supra* note 27, p. 22 et seq.

²⁹ For the characterization as specific anti-abuse provision, see also Züger, *supra* note 20, p. 561; Tumpel, *supra* note 9, p. 193; Terra and Wattel, *supra* note 11, p. 479.

³⁰ The wordings of the directives do not require the conditions for qualifying a company of a Member State to be satisfied within one tax jurisdiction; see Terra and Wattel, *supra* note 11, p. 480, p. 535 and p. 617.

³¹ Art. 2(1)(b) Parent-Subsidiary Directive, Art. 3(a)(ii) Interest and Royalty Directive and Art. 3(b) Merger Directive.

the subjective scope because they could be used in tax planning and avoidance schemes,³² as they would easily gain access to the directives from outside the Community.

Nevertheless, the fundamental freedoms fully apply to situations outside the subjective scope of a directive.³³ Being secondary law derived from the EC Treaty under Art. 249(1), directives cannot effectively restrict the application of the fundamental freedoms enshrined in the latter.³⁴

Due to the wide range of fundamental freedom protection, situations in the area of direct taxation can simultaneously fall under the freedom of establishment and the free movement of capital.³⁵ However, instead of examining both overlapping fundamental freedoms the ECJ bases its decisions on the fundamental freedom that is predominantly or primarily relevant.³⁶ Thus, no protection under the other freedom can be offered if there is no restriction to the predominant one or a restriction of the latter is justified. Restrictions under the other freedom are regarded as “an

³² Terra and Wattel, *supra* note 11, p. 479.

³³ ECJ, Advocate General Mazák’s Opinion, 18 December 2008, Case C-303/07 *Aberdeen Property Fininvest Alpha* [2009] ECT-0000, para. 23; Kofler, *supra* note 13, in print; regarding the objective scope the ECJ held in *ACT Group Litigation* that the “mere fact that, for holdings to which Directive 90/435 does not apply, it is for the Member States to determine whether, and to what extent, a series of charges to tax and economic double taxation are to be avoided [...], does not of itself mean that the Member States are entitled to impose measures that contravene the freedoms of movement guaranteed by the Treaty” (ECJ, 12 December 2006, Case C-374/04 *ACT Group Litigation* [2006] ECR-11673, para. 54); see also ECJ, 12 December 2006, Case C-446/04 *FII Group Litigation* [2006] ECR-11753, para. 68; ECJ, 8 November 2007, Case C-379/05 *Amurta* [2007] ECR-9569, paras. 21–23.

³⁴ Kofler and Toifl, “Austria’s Differential Treatment of Domestic and Foreign Intercompany Dividends Infringes the EU’s Free Movement of Capital”, 45 *European Taxation* 6 (2005), p. 236, with further references.

³⁵ Panayi, “The Fundamental Freedoms and Third Countries: Recent Perspectives”, 48 *European Taxation* 11 (2008), p. 573; Kofler, “Kapitalverkehrsfreiheit, Kontrollbeteiligungen und Drittstaaten”, *taxlex* (2008), p. 326; Mühlehner, “Controlling shareholdings and free movement of capital in relation to third countries”, *Steuer und Wirtschaft International* (2007), p. 523; Zorn, “EG-Grundfreiheiten und dritte Länder”, in: Quantschnigg, Wiesner and Mayr (Eds.), *Steuern im Gemeinschaftsrecht, Festschrift für Wolfgang Nolz* (Vienna: LexisNexis, 2008), p. 212.

³⁶ ECJ, 3 October 2006, Case C-452/04 *Fidium Finanz* [2006] ECR-9521, para. 48; ECJ, 12 September 2006, Case C-196/04 *Cadbury Schweppes* [2006] ECR-7995, para. 33; ECJ, 13 March 2007, Case C-524/04 *Test Claimants in the Thin Cap Group Litigation* [2007] ECR-2107, para. 34; ECJ, 26 June 2008, Case C-284/06 *Burda* [2008] ECR-0000, paras. 68–75; for an closer analysis see Panayi, *supra* note 35, p. 572 et seq.; Cordewener, Kofler and Schindler, “Free Movement of Capital, Third Country Relationships and National Tax Law: An Emerging Issue before the ECJ”, 47 *European Taxation* 3 (2007), pp. 113–114; Cordewener, Kofler and Schindler, “Free Movement of Capital and Third Countries: Exploring the Outer Boundaries with *Lasertec, A and B and Holböck*”, 47 *European Taxation* 8/9 (2007), pp. 372–374; Kofler, *supra* note 35, p. 330; Zorn, *supra* note 35, pp. 213–215 critical of this approach, see Stähl, “Free movement of capital between Member States and Third Countries”, 13 *EC Tax Review* (2004), p. 49.

unavoidable consequence".³⁷ This has, in particular, important implications for third-country nationals, as the free movement of capital tends to be subordinate under this approach.³⁸

Hence, the fundamental freedom that is primarily affected has to be determined in every particular case. According to Art. 43(2) EC Treaty, the freedom of establishment must include "*the right to take up and pursue activities as self-employed persons and to set up and manage undertakings*". According to the ECJ's case law, this requires a "*definite influence over the company's decisions [...] to determine its activities*".³⁹ Even though the exact participation threshold is unclear, the Court held that a participation of 25%⁴⁰ is sufficient to grant a "*definite influence*" and therefore the freedom of establishment predominantly applies, while a participation of 10%⁴¹ falls under the free movement of capital.⁴²

Under the fundamental freedoms even tax planning aimed explicitly at taking advantage of a lower tax burden by transferring economic activities in another Member State is in itself not abusive.⁴³ Member States should therefore be obliged to grant third-country dual resident companies outside the subjective scope of the direct tax directives at least the same benefits as those granted to domestic companies in comparable situations, subject to the condition that residence within the Community does not constitute a "*wholly artificial arrangement*" within the meaning of *Cadbury Schweppes*.⁴⁴

In situations where the free movement of capital is (primarily) affected, the same could even hold true for residence in a third State.⁴⁵ As regards third country sit-

³⁷ ECJ, 3 October 2006, Case C-452/04 *Fidium Finanz* [2006] ECR-9521, para. 48: "*As regards the free movement of capital within the meaning of Article 56 EC et seq., it is possible that by making financial services offered by companies which are established outside the European Economic Area less accessible for clients established in Germany, the rules effectively make those clients less inclined to have recourse to those services and, therefore, reduce cross-border financial traffic relating to those services. However, that is merely an unavoidable consequence of the restriction on the freedom to provide services*".

³⁸ Panayi, supra note 35, p. 572 et seq.

³⁹ ECJ, 13 April 2000, Case C-251/98 *Baars* [2000] ECR-2787, para. 22; ECJ, 12 September 2006, Case C-196/04 *Cadbury Schweppes* [2006] ECR-7995, para. 31; ECJ, 12 December 2006, Case C-374/04 *ACT Group Litigation* [2006] ECR-11673, para. 39; ECJ, 12 December 2006, Case C-446/04 *FII Group Litigation* [2006] ECR-11753, para. 39; ECJ, 13 March 2007, Case C-524/04 *Thin Cap Group Litigation* [2007] ECR-2107, para. 27; ECJ, 10 May 2007, Case C-492/04 *Lasertec* [2007] ECR-3775, para. 20; ECJ, 18 July 2007, Case C-231/05 *Oy AA* [2007] ECR-6373, para. 20; ECJ, 6 December 2007, Case C-298/05 *Columbus Container Services* [2007] ECR-10451, para. 30; Kofler, supra note 35, p. 326.

⁴⁰ ECJ, 10 May 2007, Case C-492/04 *Lasertec* [2007] ECR-3775, paras. 18–28.

⁴¹ ECJ, 12 December 2006, Case C-446/04 *FII Group Litigation* [2006] ECR-11753, paras. 58–74.

⁴² Cordewener, Kofler and Schindler, supra note 36, pp. 373–374; Kofler, supra note 35, p. 326.

⁴³ See supra note 22.

⁴⁴ ECJ, 12 September 2006, Case C-196/04 *Cadbury Schweppes* [2006] ECR-7995, para. 55.

⁴⁵ For an extensive analysis of the scope of Art. 56(1) in third-country relationships, see Cordewener, Kofler and Schindler, supra note 36, p. 109 et seq.

uations the ECJ, however, seems not to apply the same strict standards it applies to restrictions of intra-Community situations.⁴⁶ Furthermore, the “*grandfather clause*”⁴⁷ in Art. 57(1) EC Treaty provides an important exception to the protection of third-country situations regarding restrictions which already existed on 31 December 1993.⁴⁸

4. Summary

Directive shopping describes the situation in which a person “*shops*” around in an otherwise inapplicable directive, aiming to taking advantage of the directive provisions. Directive shopping is, like treaty shopping, a form of tax avoidance. The direct tax directives contain general anti-abuse provisions which grant Member States a certain discretionary power to apply domestic or treaty-based anti-abuse provisions in combating directive shopping schemes.

However, from the *Denkavit*, *VITIC* and *Voormeer* cases it can be derived that such general anti-abuse provisions cannot be relied on by Member States in situations where the directives already deal with in specific anti-abuse provisions. This is, *inter alia*, the case as regards dual residence: According to Art. 2(1)(b) Parent-Subsidiary Directive, Art. 3(b) Merger Directive and Art. 3(a)(ii) Interest and Royalty Directive, dual resident companies are excluded from directive application if such companies have one of their residences in a third State which is deemed to be the State of residence for tax treaty purposes. Within the scope of the direct tax directives dual residence in itself can therefore never be an abusive structure. Outside their scope, dual resident companies might nevertheless enjoy protection under the fundamental freedoms.

⁴⁶ Panayi, *supra* note 35, p. 579 et seq.; Cordewener, Kofler and Schindler, *supra* note 36, pp. 114–117; Peters and Gooijer, “The Free Movement of Capital and Third Countries: Some Observations”, 45 *European Taxation* 11 (2005), pp. 479–480.

⁴⁷ Also referred to as “*standstill clause*”.

⁴⁸ Panayi, *supra* note 35, pp. 577–578; Cordewener, Kofler and Schindler, *supra* note 36, pp. 117–118; Cordewener, Kofler and Schindler, *supra* note 36, pp. 375–376; Smit, “Capital movements and third countries the significance of the standstill clause ex article 57(1) EC in the field of direct taxation”, 15 *EC Tax Review* (2006), p. 203; Peters and Gooijer, *supra* note 46, pp. 477–479.