JUDGMENT OF THE COURT (Fourth Chamber)

9 July 2009

(Failure of a Member State to fulfil obligations – Indirect taxes on the raising of capital – Capital companies – Directive 69/335/EEC – Articles 2(1) and (3), 4(1) and 7 – Capital duty – Exemption – Conditions – Transfer of effective centre of management or of registered office from one Member State to another Member State – Capital duty on the capital allocated to commercial activities pursued in a Member State by branches or permanent establishments of companies established in another Member State)

In **Case C-397/07**,

ACTION under Article 226 EC for failure to fulfil obligations, brought on 27 August 2007,

Commission of the European Communities, represented by E. Gippini Fournier and M. Afonso, acting as Agents, with an address for service in Luxembourg,

applicant,

v

Kingdom of Spain, represented by B. Plaza Cruz and M. Muñoz Pérez, acting as Agents, with an address for service in Luxembourg,

defendant,

supported by:

Hellenic Republic,

intervener,

THE COURT (Fourth Chamber),

composed of K. Lenaerts, President of the Chamber, T. von Danwitz, E. Juhász (Rapporteur), G. Arestis and J. Malenovský, Judges,

Advocate General: J. Kokott,

Registrar: M. Ferreira, Principal Administrator,

having regard to the written procedure and further to the hearing on 15 January 2009,

after hearing the Opinion of the Advocate General at the sitting on 5 March 2009,

gives the following

Judgment

1 By its application, the Commission of the European Communities asks the Court for a declaration that:

– by subjecting the application of mandatory exemptions from capital duty to certain conditions,

– by imposing capital duty on the transfer to Spain of the effective centre of management or the registered office of companies which have not been subject to a similar tax in their country of origin, and

– by subjecting to capital duty capital allocated to commercial activities pursued in Spain by branches or permanent establishments of companies established in a Member State which does not apply a tax similar to that applied in Spain,

the Kingdom of Spain has failed to fulfil its obligations under Council Directive 69/335/EEC of 17 July 1969 concerning indirect taxes on the raising of capital (OJ, English Special Edition 1969 (II), p. 412), as amended by Council Directive 73/79/EEC of 9 April 1973 (OJ 1973 L 103, p. 13) and Council Directive 85/303/EEC of 10 June 1985 (OJ 1985 L 156, p. 23) ('Directive 69/335').

Legal context

Community legislation

2 In accordance with the first recital in the preamble thereto, the objective of Directive 69/335 is the promotion of the free movement of capital with a view to creating an economic union whose characteristics are similar to those of a domestic market. To that end, as evidenced by the sixth to eighth recitals in the preamble thereto, that directive aims to harmonise the duties imposed on capital raised for companies in the European Community, through the introduction of a single duty for the raising of capital, to be imposed only once within the common market and through the abolition of all other indirect duties having the same characteristics as that single capital duty.

3 Thus, Article 1 of Directive 69/335 provides that 'Member States shall charge on contributions of capital to capital companies a duty harmonised …'.

4 Article 2 of Directive 69/335 provides for a sharing of taxation powers between the Member States:

'1. Transactions subject to capital duty shall only be taxable in the Member State in whose territory the effective centre of management of a capital company is situated at the time when such transactions take place.

…

3. When the registered office and the effective centre of management of a capital company are situated in a third country, the supplying of fixed or working capital to a branch situated in a Member State may be taxed in the Member State in whose territory the branch is situated.'

5 Article 4(1) of Directive 69/335 lists the transactions which are subject to capital duty, including both the formation of a capital company and the increase of its capital, and:

'(g) the transfer from a Member State to another Member State of the effective centre of management of a company, firm, association or legal person which is considered in the latter Member State, for the purposes of charging capital duty, as a capital company, but is not so considered in the other Member State;

(h) the transfer from a Member State to another Member State of the registered office of a company, firm, association or legal person, whose effective centre of management is in a third country and which is considered in the latter Member State, for the purposes of charging capital duty, as a capital company, but is not so considered in the other Member State'.

6 The original version of Article 7 of Directive 69/335 provided as follows with respect to the rate of capital duty:

'1. Until the entry into force of the provisions to be adopted by the Council in accordance with paragraph 2:

(a) the rate of capital duty may not exceed 2% or be less than 1%;

(b) this rate shall be reduced by 50% or more when one or more capital companies transfer all their assets and liabilities, or one or more parts of their business to one or more capital companies which are in the process of being formed or which are already in existence.

…'

7 The latter reduction in the capital duty, which is subject to certain conditions, is provided for with respect to transactions commonly known as 'restructuring of capital companies'.

8 Council Directive 73/80/CEE of 9 April 1973 fixing common rates of capital duty (OJ 1973 L 103, p. 15) reduced, with effect from 1 January 1976, the rate of capital duty referred to in the original version of Article 7(1)(b), in respect of restructuring transactions for capital companies, fixing it at 0% to 0.50%.

9 Directive 73/79 added a subparagraph (bb) to the abovementioned Article 7(1), under which the Member States may extend the application of the reduced rate of capital duty to transactions equivalent to the abovementioned restructuring transactions, namely ' where a capital company which is in the process of being formed or which is already in existence acquires shares representing at least 75% of the issued share capital of another capital company'.

10 The second recital in the preamble to Directive 73/79 states that in such a case a company acquires a proportion of the shares in another company such that it obtains complete control of such other company.

11 Directive 85/303, in stating in the fourth recital in the preamble thereto that 'there should be mandatory exemption for the transactions currently subject to the reduced rate of capital duty', amended Article 7 of Directive 69/335 in the following manner:

> '1. Member States shall exempt from capital duty transactions … which were, as at 1 July 1984, exempted or taxed at a rate of 0.50% or less.
>
> …
>
> 2. Member States may either exempt from capital duty all transactions other than those referred to in paragraph 1 or charge duty on them at a single rate not exceeding 1%.
>
> …'

National legislation

Tax treatment of restructuring transactions involving capital companies

12 Article 1(1)(2) of the Spanish Law on capital transfers and documented legal transactions (Ley del Impuesto sobre Transmisiones Patrimoniales y Actos Jurídicos Documentados), enacted by Royal Legislative Decree (Real Decreto Legislativo) No 1/1993 of 24 September 1993 (BOE (Spanish Official Journal) of 20 October 1993) ('the tax law'), imposes an indirect tax on certain transactions involving commercial companies. Under Article 19(1)(1) of the tax law, the transactions subject to the tax are the formation of a company, increasing or reducing a company's capital, mergers and demergers, and the winding-up of companies.

13 As regards tax-exempt transactions, Article 45, Part I(b)(10) of the tax law, in conjunction with Article 21 thereof and the second additional provision of the consolidated version of the Spanish Law on corporation tax (Disposición Adicional Segunda del texto Refundido de la Ley del Impuesto sobre Sociedades), enacted by Royal Legislative Decree (Real Decreto Legislativo) No 4/2004 of 5 March 2004 (BOE of 11 March 2004) ('the law on corporation tax'), provides that transactions involving merger, demerger, the transfer of parts of undertakings and the exchange of shares, defined in Chapter VIII, Title VII, of the law on corporation tax, which establishes a special regime in this connection, are exempt from the duty, provided that this regime is in each case applicable to the transaction concerned.

14 Article 96 of the law on corporation tax, entitled 'Applicability of the tax regime', sets out the conditions governing the applicability of this special regime. It provides:

> '1. In order for the regime established in this Chapter to be applicable, there must have been an election to opt for the regime and the following conditions must have been satisfied:

(a) in cases of merger and of demerger, that option must have been included within the proposal and the agreements for merger or demerger of the transferor and transferee undertakings, which are domiciled for tax purposes in Spain.

…

(b) with regard to contributions in kind, the option must be exercised by the transferee undertaking in the resolution approving the takeover or merger, or, failing that, in the authentic instrument witnessing the transaction or contract in question.

…

(c) in cases involving a share exchange, the option must be exercised by the transferee undertaking in the resolution approving the takeover or merger, or, failing that, in the authentic instrument by which the transaction or contract in question is constituted. In cases involving a public offer for the acquisition of shares, the option must be exercised by the body of the company having the authority to implement the transaction and must appear in the information documents relating to the offer.

…

In every case, the exercise of the option must be notified to the Ministry of Finance in the form and within the period laid down by the applicable provisions.

2. The regime laid down by this Chapter shall not apply where the principal object of the transaction entered into is tax avoidance or evasion. In particular, the regime shall not apply where the transaction is entered into otherwise than for valid economic reasons, such as the restructuring or rationalisation of the activities of the undertakings involved in the transaction, but solely in order to obtain a tax advantage.

…'

<u>Transfer of the effective centre of management or of the registered office of a capital company</u>

15 Article 19(3) of the tax law provides that liability to the tax is to arise in cases involving:

'The transfer of the place of the centre of effective management or the registered office of a company to Spain, where neither of these was previously located in a Member State … or where the undertaking was not subject, in a Member State, to a tax equivalent to the duty provided for in this Title.'

<u>Taxation in respect of branches or permanent establishments of a capital company established in another Member State</u>

16 Article 20 of the tax law provides:

‘Undertakings which carry out, through branches or permanent establishments, commercial transactions in Spain and whose registered office or centre of effective management are located in a country which does not belong to the … Community or are located in such a country without the undertaking being subject to a tax equivalent to the duty provided for in this Title, shall be taxed in the same way and under the same conditions as Spanish undertakings as regards the amount of their capital which is allocated to those transactions.’

Pre-litigation procedure

17 As it had doubts as to whether the abovementioned provisions of the Spanish legislation complied with the requirements of Directive 69/335, the Commission addressed a letter of formal notice to the Kingdom of Spain on 19 December 1993 and, on 18 October 2004, it sent a supplementary letter of formal notice. The Spanish authorities replied by letters of 3 February and 24 November 2004 respectively. As those replies confirmed the Commission’s initial doubts, on 13 July 2005 it sent the Kingdom of Spain a reasoned opinion. Following the response from the Spanish authorities to that reasoned opinion on 18 July 2006, the Commission’s complaints materialised and led to the present proceedings.

The action

The first complaint

18 The first complaint relates to the conditions laid down in Article 96 of the law on corporation tax, which must be satisfied for the relevant companies to be able to benefit from the special tax exemption regime provided for in Chapter VIII, Title VII, of that same law. The Commission claims that those conditions are unlawful with respect to the transactions which must be exempt from the capital duty under Directive 69/335.

19 Despite the negative general formulation of this complaint, the reasoning in the order for reference makes it clear that it relates to transactions coming under Article 7(1)(b) and Article 7(1)(bb) of Directive 69/335, as amended by Directives 73/79 and 73/80, before the amendment introduced by Directive 85/303. The content of those provisions, in the light of the reference in Article 7(1), as amended by the latter directive, to the situation existing as at 1 July 1984, remains relevant even after the entry into force of that directive.

20 It should be recalled at the outset that, in Case C-366/05 *Optimus – Telecomunicações* [2007] ECR I-4985, paragraphs 25 to 33, the Court held that, with respect to a State such as in the present case the Kingdom of Spain, which acceded to the Community with effect from 1 January 1986, the date 1 July 1984, which is taken as the reference date for the purposes of the mandatory exemption provided for in Article 7(1) of Directive 69/335, as amended by Directive 85/303, also applies in respect of Spain. At the hearing, the Agent for the Kingdom of Spain referred to a legislative text concerning transactions involving capital companies which are taxed in Spain as at 1 July 1984. As the parties were asked by the President of the bench to state their position on that information which could constitute fresh evidence, they accepted that the Court rule on the case on the basis of the written observations lodged with it.

21 As regards transactions coming under Article 7(1)(b), the rate of capital duty had been reduced with binding effect as from 1 January 1976 by Directive 73/80 and fixed at 0% to 0.50%. Accordingly, following the amendment to Article 7(1) by Directive 85/303, the transactions in question were, as from 1 January 1986, mandatorily exempted from capital duty. The Commission's complaints therefore relate to those transactions.

22 By contrast, transactions coming under Article 7(1)(bb), for which a reduction in capital duty was, at the time of the introduction of that provision by Directive 73/79, merely optional, were mandatorily exempted from capital duty under Directive 85/303 only if they were exempted or taxed at a rate equal to or lower than 0.50% as at 1 July 1984, which reference date is also applicable for the Kingdom of Spain, following *Optimus – Telecomunicações*. On that date, the transactions in question were not all mandatorily subject to the same rate of capital duty giving rise to a mandatory exemption under Directive 85/303.

23 In this case, the Commission has not adduced any evidence establishing that the transactions coming under Article 7(1)(bb) of Directive 69/335 were exempted or taxed at a rate equal to or lower than 0.50% as at 1 July 1984 in Spain, with the result that those transactions cannot be considered to be mandatorily exempt from capital duty under Directive 69/335. Consequently, it is appropriate to dismiss the first complaint in so far as it relates to Article 7(1)(bb) of that directive and to pursue the examination of the complaint as regards the transactions referred to in Article 7(1)(b).

24 The Commission's specific complaint in this respect is that, in accordance with the Spanish legislation, in order to benefit from the tax exemption for the transactions in question provided for in Article 1(1)(2) of the tax law, the company concerned must formally opt for the special exemption regime introduced in Chapter VIII, Title VII, of the law on corporation tax, whereas Directive 69/335, following the amendment introduced by Directive 85/303, provides for a mandatory exemption of those transactions, without that exemption being subject to compliance with any conditions such as a formal opting for the special exemption regime. Moreover, the company concerned must inform the Ministry of Finance of the exercise of the option, which is an additional obstacle to the application of the exemption.

25 The Kingdom of Spain, whilst not disputing that those transactions are in the category of transactions which must necessarily be exempted, argues, in essence, that opting for the special exemption regime does not impose any material burden on the company in question and is merely a minimum condition of a purely formal nature. The only substantive condition for the application of that regime is that the principal object of the transaction in question must not be tax avoidance or evasion. The obligation to notify the tax authorities of the transaction is precisely to allow them to check that the underlying economic reasons for the transaction are sound and justify its taking place.

26 That argument cannot be accepted.

27 Directive 69/335, with a view to promoting the free movement of capital through the harmonisation and, so far as possible, the gradual abolition of capital duty, has provided for an exemption from capital duty for those transactions which come under Article 7(1)(b) thereof. That exemption is mandatory and unconditional and, for the companies

concerned, a right the exercise of which must be ensured at national level in a straightforward and unambiguous manner.

28 To incorporate that right into a special exemption regime and make the exercise thereof subject to a formal opting-in is liable to give rise to doubts and ambiguities on the part of the companies concerned as to the origins of that right and the conditions for exercising it, thereby making it incompatible with the system established by Directive 69/335. Moreover, the obligation to opt for that special regime is not a mere formality, as that option must be notified to the tax authorities in the manner and by the time-limits laid down in national legislation. That double obligation of electing the option and notifying it, imposed as a condition for exercising a right granted unconditionally by Directive 69/335, is an obstacle incompatible with that directive.

29 The special regime in dispute cannot be justified by the objective of combating tax avoidance and evasion. According to the Court's settled case-law, since Directive 69/335 harmonises exhaustively the cases in which the Member States may impose capital duty and does not contain any provision expressly authorising the Member States to take general measures to prevent tax avoidance, the Member States can prevent the application of Community law only in specific circumstances entailing an abusive or fraudulent practice (Case C-178/05 *Commission* v *Greece* [2007] ECR I-4185, paragraph 32).

30 Consequently, as rightly observed by the Commission, such measures cannot be founded on a general suspicion of tax evasion. They may be adopted only on a case-by-case basis, in order to put a stop to wholly artificial arrangements which do not reflect economic reality and aim to avoid the tax normally payable (see, to that effect, Case C-251/06 *ING. AUER* [2007] ECR I-9689, paragraph 44), it being understood that, in such cases, the competent national authorities bear the burden of proving the fraudulent or artificial nature of the transaction in question.

31 As the Kingdom of Spain has not established that its legislation is aimed solely at the wholly artificial arrangements as contemplated above, the Court finds that the Commission's complaint is well founded as regards transactions coming under Article 7(1)(b) of Directive 69/335.

The second complaint

32 The second complaint relates to Article 19(3) of the tax law, which provides that capital duty will be incurred in the event of the transfer to Spain of the place of the centre of effective management or the registered office of a capital company which was previously located in a Member State which did not charge a capital duty equivalent to that provided for in the Spanish legislation. The Commission argues that Article 4 of Directive 69/335, which contains an exhaustive list of the transactions subject to capital duty, does not provide that a transaction such as that provided for in that provision of the tax law is to give rise to capital duty and that, therefore, such a duty is thereby precluded.

33 The Kingdom of Spain replies that that provision is aimed at preventing the provisions of Directive 69/335 from being used to circumvent the application of the Spanish tax regime and is therefore justified by the objective of combating tax avoidance and

evasion. One example of this is capital companies which plan from the beginning to pursue their activities in Spain but establish themselves in a Member State where their corporate form is not subject to a capital duty similar to that applicable in Spain.

34 The defendant's line of argument cannot be accepted.

35 It should be noted, first, that it is clear from Article 4(1)(g) and (h) of Directive 69/335 that capital duty is chargeable on transfers, from a Member State to another Member State, of the effective centre of management or registered office of companies which are considered in the latter Member State, for the purposes of charging capital duty, to be capital companies, but are not so considered in the former Member State. Consequently, the only criterion to which that provision makes the application of capital duty subject in the event of such a transfer is that of whether the entity in question is a 'capital company' in the Member State of origin. Thus such a transfer may not be made subject to capital duty when the entity in question is considered a 'capital company' in the Member State of origin and in the host Member State (see, to that effect, *Commission* v *Greece*, paragraphs 26, 27 and 29).

36 Moreover, as observed by the Advocate General in point 62 of her Opinion, the question of which companies are to be regarded as 'capital companies' for the purposes of applying capital duty is regulated in a mandatory and uniform fashion for all Member States by Article 3(1) of Directive 69/335.

37 Article 19(3) of the tax law makes the application of capital duty in Spain, in the event of transfer to that Member State of the effective centre of management or of the registered office of a capital company, subject to the criterion of whether that company is or is not subject to a similar duty in the Member State of origin. That criterion of 'taxation' or of being 'subject to' duty in the Member State of origin does not comply with the abovementioned criterion, laid down in Article 4(1)(g) and (h) of Directive 69/335, and thus allows for taxation by way of capital duty in cases not provided for by that directive. Since that directive harmonises in an exhaustive manner how Member States may tax the transfer of the registered office or the effective centre of management, that provision of the tax law is incompatible with Article 4(1)(g) and (h) of Directive 69/335.

38 That provision is also contrary to the general system established by Directive 69/335. The fact that a Member State has exercised the option provided for in that directive by abolishing capital duty does not mean that, if the effective centre of management of a capital company is transferred from one Member State to another Member State, the latter State may automatically make that transaction subject to capital duty (see, to that effect, *ING. AUER*, paragraphs 34 and 35).

39 Secondly, Article 19(3) of the tax law is based on a general presumption of tax evasion, as that provision contains measures which are applied automatically and without distinction. For the reasons set out in paragraphs 29 and 30 of this judgment and in keeping with the Court's settled case-law referred to in those paragraphs, that provision may not be justified by the objective of combating tax avoidance and evasion. More specifically, exercise of a right created by Community law, such as establishment of a company in another Member State or transfer of its effective centre of management or

registered office, cannot in itself warrant suspicion of abuse (*Commission* v *Greece*, paragraph 32).

40 The second complaint must therefore be held to be well founded.

The third complaint

41 In this complaint, the Commission argues that Article 20 of the tax law leads to the capital duty being applied, in respect of the share of the capital which is allocated to commercial transactions in Spain, to any branch or permanent establishment of a capital company whose registered office or effective centre of management is situated in another Member State which does not charge a duty similar to that charged in Spain. The Commission maintains that such a form of taxation is contrary to the allocation of tax competences between the Member States as provided for in Article 2(1) of Directive 69/335.

42 Under Article 20 of the tax law, undertakings which carry out, through branches or permanent establishments, commercial transactions in Spain and whose registered office or centre of effective management are located in a country which does not charge a tax equivalent to that charged in Spain, are to be taxed in the same way and under the same conditions as Spanish undertakings as regards the amount of their capital which is allocated to those transactions.

43 It is clear from the wording of that provision, which refers to 'undertakings' carrying out commercial transactions in Spain through branches or permanent establishments, that the Spanish legislation provides for the taxation of capital companies which have their effective centre of management in other Member States to which the branches or permanent establishments situated in Spain belong, in respect of the amount of their capital which is allocated to the transactions performed by the branches or permanent establishments in question in Spain.

44 The Kingdom of Spain does not dispute that the present case involves a capital duty charged in Spain on the transactions in question. The defendant merely states, in its defence, that the provision at issue is justified by the objective of combating tax avoidance, consisting in establishing a company in a Member State which does not charge a tax similar to the Spanish tax, then establishing immediately afterwards a permanent establishment or branch in Spain from which that company effects commercial transactions in Spain.

45 The taxation of such transactions by capital companies having their effective centre of management in another Member State is, however, contrary to Article 2(1) of Directive 69/335, which provides that transactions which are subject to capital duty may be taxed only in the Member State in which the capital company's effective centre of management is situated at the time of those transactions.

46 That taxation, which is a measure of general application imposed without distinction, cannot be justified by the objective of combating tax avoidance and evasion, for the reasons set out in paragraphs 29 and 30 of this judgment.

47 The Commission's third plea is accordingly well founded.

48 In the light of all the foregoing, the Court finds that:

– by making the exemption from capital duty for the transactions referred to in Article 7(1)(b) of Directive 69/335 subject to the conditions laid down in Article 96 of the law on corporation tax,

– by subjecting to capital duty the transfer, from a Member State to Spain, of the effective centre of management or the registered office of capital companies which have not been subject to a similar tax in their country of origin, and

– by subjecting to capital duty capital allocated to commercial activities pursued in Spain by branches or permanent establishments of companies established in a Member State which does not apply a similar tax,

the Kingdom of Spain has failed to fulfil its obligations under Directive 69/335.

49 The action is dismissed as to the remainder.

Costs

50 Under Article 69(2) of the Rules of Procedure, the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the Commission applied for costs to be awarded against the Kingdom of Spain and the latter has been unsuccessful in its main pleas, the Kingdom of Spain must be ordered to pay the costs.

On those grounds, the Court (Fourth Chamber) hereby:

1. Declares that:

– by making the exemption from capital duty for the transactions referred to in Article 7(1)(b) of Council Directive 69/335/EEC of 17 July 1969 concerning indirect taxes on the raising of capital, as amended by Council Directive 73/79/EEC of 9 April 1973, Council Directive 73/80/EEC of 9 April 1973 and Council Directive 85/303/EEC of 10 June 1985, subject to the conditions laid down in Article 96 of the second additional provision of the consolidated version of the Spanish Law on corporation tax (Disposición Adicional Segunda del texto Refundido de la Ley del Impuesto sobre Sociedades), enacted by Royal Legislative Decree No 4/2004 of 5 March 2004,

– by subjecting to capital duty the transfer, from a Member State to Spain, of the effective centre of management or the registered office of capital companies which have not been subject to a similar tax in their country of origin, and

– by subjecting to capital duty capital allocated to commercial activities pursued in Spain by branches or permanent establishments of companies established in a Member State which does not apply a similar tax,

the Kingdom of Spain has failed to fulfil its obligations under Directive 69/335, as amended by Directives 73/79, 73/80 and 85/303;

2. Dismisses the action as to the remainder;

3. Orders the Kingdom of Spain to pay the costs.