The (Un)remarkable Lexel Case in Dutch Case Law

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1. Interest Deduction under Dutch Tax Law

Interest is – generally – deductible, unless:

- the loan is akin to equity (three exceptions)
- **the loan as such / the interest amount is not at arm's length**
- **Article 10a applies**
- Article 10b applies (loans with special conditions)
- interest expenses exceed 30% percent of EBITDA

- fraus legis

2. The TP Challenge: a Heavy Burden of Proof for the Tax Inspector

- Tax authorities invoke OECD TP Guidelines to recharacterize loan (debt/equity structure) and argue only shareholder interests are served.
- Supreme Court only accepts ‘three exceptions’ (see HR 25 November 2011, 08/05323, BNB 2012/37) (note the ‘non-businesslike loan’ doctrine)
- RB Noord-Holland 26 July 2022, AWB-18-2897:
  - Taxpayer has TP documentation; tax inspector argues no third party would have granted the loan. Tax inspector scrutinizes key points in the documentation, no own TP report. Does not satisfy burden of proof why full denial of interest.
- Choice to fund with equity or debt is not restricted by ‘total profit principle’ / ‘transfer pricing’.

3. Article 10a for (Smart!) Dummies

- Comes after Article 8/8b (covers at arm's length interest)
- Purpose (X BV and Y BV (C-398/16 and C-399/16, par. 34)):

  "seeks to prevent the Netherlands tax base being eroded by contrived intra-group financial arrangements"
- Applies to:
  - Interest paid to related entities/collaborative groups
  - Relating to certain transactions (e.g. share acquisitions – internal AND external)
- Affects payments to both Dutch- and foreign-resident creditors (note: fiscal unity effect)
- Two escapes:
  - the interest is subject to a reasonable levy
  - there are sound business reasons for both the loan AND the associated transaction
- If applicable: a full denial of deduction

4. Article 10a is alive

- Final Supreme Court case after X BV and Y BV (C-398/16 and C-399/16), HR 19 October 2018, nr. 15/00194, BNB 2019/17
- Final Credit Suisse Case, HR 22 March 2019, nr. 18/02329 et seq., BNB 2019/98
- HR 9 July 2021, nr. 19/05112, BNB 2021/136 (AON)
- HR 16 July 2021, nr. 19/02596, BNB 2021/137 (Hunkemöller)
- HR 15 July 2022, nr. 20/02096, BNB 2022/112
- HR 15 July 2022, nr. 20/03946, BNB 2022/113
- HR 2 September 2022, nr. 20/03948

In short: Article 10a is alive due to:

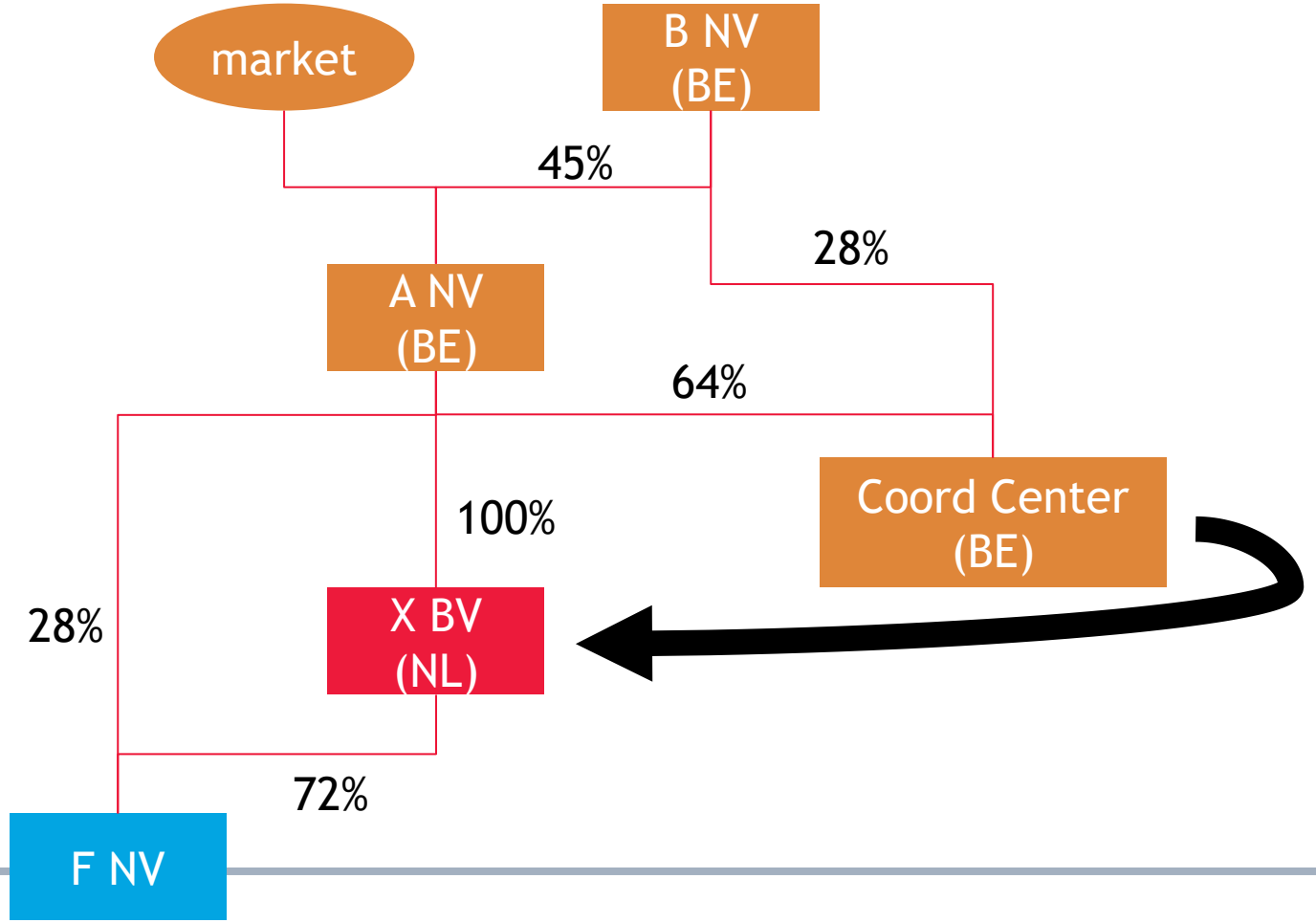
- 'artificial rerouting'-doctrine
- collaborative group

5. Discussion of Lexel in Dutch Case Law

- Opinion A-G Wattel, 29 June 2022, Case 20/03946
- Opinion A-G Wattel, 29 June 2022, Case 20/03948
- Opinion A-G Wattel, 31 August 2021, Case 21/00299
- Gerechtshof Amsterdam, 30 September 2021, Case 19/00872
- Opinion A-G Wattel, 24 May 2022, Case 21/04746
- Rechtbank Noord-Holland, 26 July 2022, Case AWB – 18 – 2897
- Hoge Raad, 2 September 2022, Case 20/03948

In case 20/03946, the Supreme Court concluded no 'rerouting' of funds as the PEC-holders did not individually have an interest of 1/3 in the taxpayer. Hence, no Article 10a.

6. A-G Wattel's Opinion in the Belgian Coord. Center Case



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- Lexel's par. 56: if conditions are at arm's length, no abuse? No: creation can be problematic (see Thin Cap Glo, par. 81).
- In Lexel: transaction and loan as such (apparently) legit. Swedish rule categorically denied interest payment to loss-making group companies. Within Sweden: group contribution. Only the conditions of the loan remained.
- In BCC case: financing structure as such is problematic
- Will CJEU recognise: different rules -> different purposes -> different escapes?
  - 'Arm's length' no escape to rule as Article 10a
- Lexel does not help taxpayer in BCC:
  - No discrimination
  - Purpose of the Swedish rules (see Lexel, par. 52,53) ≠ Article 10a

7. The Supreme Court in the Belgian Coord. Center Case

- Par. 3.7.2: arbitrary loan arrangements without sounds reasons can be artificial arrangements, even when loan conditions of the loan are at arm's length. Arm's length or not: equal risk of tax avoidance.

- Par. 3.7.4: CJEU has not said that an arrangement cannot be artificial when conditions are at arm's length.

- 3.7.5: the view in 3.7.4 not unanimously shared in literature (referring Lexel, par. 56). Comparison of Lexel, par. 56 in different language versions. Sufficient doubt if Supreme Court's view is correct.

7. The Supreme Court in the Belgian Coord. Center Case

- 1. Do Articles 49, 56, and/or 63 TFEU preclude Art. 10a where there is:
  - a. a loan to a related entity
  - b. linked to the acquisition or increase of an interest in a related entity, and
  - c. where the loan must be considered part of a wholly artificial arrangement,

"irrespective whether the loan as such is agreed upon at arm's length conditions"

- 2. If no: do Articles 49, 56 and/or TFEU preclude Art. 10a for fully denying interest deduction, even when the interest does not exceed what is at arm's length?

- 3. Relevant whether internal or external acquisition?

8. Observations

- The questions are ‘framed’.
- They will not provide guidance on whether financing through a BCC is wholly artificial.
- Clear description of the purpose of Article 10a (not to prevent deduction of excessive interest)
- *De facto* non-discrimination analysis
- Remarkably formulated ‘trigger’ for referring to CJEU
- Defensible position to not apply Article 10a?