The CJEU finds a Swedish anti-abuse rule, which denies the deduction for interest paid to non-resident associated companies, to be contrary to EU law

On 20 January 2021, the Court of Justice of the European Union ("CJEU") issued its judgment in case C-484/19, *Lexel AB*. The case concerned the deduction for interest paid by a Swedish company ("Lexel") to a French associated company ("BF").

Lexel acquired the shares in a Belgian company ("SESI") from a Spanish company ("SEE") that was part of the same group of Lexel. In order to finance that acquisition, Lexel took out a loan from BF, the group finance company. BF offset the interest received against the losses arising from the group's business activities in France. The Swedish tax authorities denied the interest deduction on the basis of the domestic legislation providing that interest expenses incurred vìs-à-vìs an associated company belonging to the same group may not be deducted if the main reason for entering the loan agreement is to ensure a substantial tax benefit at group level. In this respect, Lexel stated that the reason for acquiring the shares in SESI from SEE was that the latter company needed capital in connection with its acquisition of another company from third parties. Lexel also highlighted that SEE had already taken out some loans for this purpose.

The CJEU was asked to clarify if the freedom of establishment does preclude the application of the above-mentioned legislation. The CJEU agreed that, according to Swedish applicable tax law, while interest paid to a company established in another Member State would be deductible if a substantial tax benefit would not have been deemed to exist, such condition was not required for the purposes of deducting the interest paid to a Swedish company. On those grounds, the CJEU concluded that the Swedish anti-abuse rule constitutes a difference in tax treatment that may lead to a restriction of the freedom of establishment.

In this respect, the CJEU first clarified that the situation of a company paying interest to a resident associated enterprise should be regarded as comparable to the situation of a company paying interest to a non-resident associated enterprise.

Second, in the CJEU's view, the restriction at stake was not justified by overriding reasons of general interest. The Court found that Sweden may not invoke the objective of combating fraud and tax evasion. Indeed, for such justification to apply, the relevant domestic legislation must be specifically targeted at preventing the creation of wholly artificial arrangements which do not reflect economic reality, with a view to escaping the tax normally due on the profits generated by activities carried out on the national territory. In the case at stake, the Swedish anti-abuse rule did not pursue

such an objective, given that it had a broader scope and might apply whenever a loan was mainly taken out for tax purposes (indeed its scope also included operations compliant with market conditions). Interestingly, the CJEU stressed (at para. 55) that the mere fact that a company seeks to deduct interest in a cross-border situation cannot, in the absence of any artificial transfer, justify a measure adversely affecting the freedom of establishment provided for in Article 49 TFEU. The CJEU also clarified (at para. 69 and para. 70) that the need to safeguard a balanced allocation of taxing rights could not be invoked as a justification, insofar as the conditions of an intra-group cross-border transaction are in line with market conditions.

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