REPORT FOR THE HEARING

in Case E-3/21

REQUEST to the Court under Article 34 of the Agreement between the EFTA States on the Establishment of a Surveillance Authority and a Court of Justice by Oslo District Court (*Oslo tingrett*), in the case between

PRA Group Europe AS

and

the Norwegian Government, represented by the Tax Administration,

concerning the interpretation of the rules on freedom of establishment, in particular the interpretation of Article 31 of the Agreement on the European Economic Area, read in conjunction with Article 34 thereof, in relation to the Norwegian limited interest deduction rule and group contribution rules.

I Introduction

1. By letter of 1 July 2021, registered at the Court on the following day, Oslo District Court (*Oslo tingrett*) made a request for an advisory opinion in the case pending before it between PRA Group Europe AS ("PRA") and the Norwegian Government, represented by the Tax Administration.

2. The case referred concerns the validity of the Tax Appeal Board's decision of 24 June 2020, by which for the Norwegian fiscal years 2014 and 2015 (the "material time") a tax deduction for interest paid by PRA Group Europe Subholding AS on debt to affiliated parties was limited in accordance with Section 6-41 of the Norwegian Act No 14 of 26 March 1999 on taxation of assets and income (*Lov om skatt av formue og inntekt av 26. mars 1999 nr. 14 (skatteloven)*) (the "Norwegian Tax Act"). PRA Group Europe Subholding AS was merged into PRA in November 2016. In the course of the national proceedings, the question has arisen whether the limitation of deductibility under Section 6-41 of the Norwegian Tax Act, read in conjunction with Sections 10-2 to 10-4 of the Norwegian Tax Act on group contributions, is compatible with Article 31 of the Agreement on the European Economic Area ("EEA Agreement" or "EEA"), read in conjunction with Article 34 EEA.

II Legal background

EEA law

3. Article 31(1) EEA reads:

> *Within the framework of the provisions of this Agreement, there shall be no restrictions on the freedom of establishment of nationals of an EC Member State or an EFTA State in the territory of any other of these States. This shall also apply to the setting up of agencies, branches or subsidiaries by nationals of any EC Member State or EFTA State established in the territory of any of these States.*
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> *Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of Article 34, second paragraph, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of Chapter 4.*

4. Article 34 EEA reads:

> *Companies or firms formed in accordance with the law of an EC Member State or an EFTA State and having their registered office, central administration or principal place of business within the territory of the Contracting Parties shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of EC Member States or EFTA States.*
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> *'Companies or firms' means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit-making.*

National law

5. At the material time, the Norwegian Tax Act contained the following provisions.

6. Section 6-40(1) of the Tax Act laid down the general rules on deduction of debt interest payments.

7. Section 6-41 of the Norwegian Tax Act entitled "Limitation of interest deduction between affiliated parties" read, in extract: [1]

[1] All translations of national law are unofficial.

(1) The rules in this Section regarding limitation of deduction of net interest expenses on debt to affiliated individuals, companies or entities shall apply to:

a. companies and entities as referred to in first paragraph of Section 2-2;

...

(2) Net interest expenses under this section shall include interest expenses as referred to in Section 6-40, less interest income. Profit and loss on composite bonds that are not to be broken down into a bond part and a derivate part for tax purposes, shall in their entirety be considered to be interest income or interest expenses. The same applies to profit and loss on financial assets issued at a higher or lower price than its redemption value. Profit and loss as referred to in the preceding sentence are not considered to be interest income or interest expenses for a holder who has acquired the debt instrument in the secondary market.

(3) If net interest expenses exceed NOK 5 million, they may not be deducted for the part that exceeds 30% of general income or uncovered loss for the year before the limitation of deductions under this section, plus interest expenses and tax depreciation, and less interest income. The disallowance of interest deduction pursuant to the preceding sentence shall be done only for an amount up to the amount of net interest expenses on debt to affiliated individuals, companies or entities. No deduction shall be given for any additional losses carried forward, see Section 14-6, or group contribution, see Section 10-4, after an interest deduction has been disallowed under this paragraph. If net interest expenses for the year do not exceed NOK 5 million, but the sum of net interest expenses for the year and net interest expenses carried forward from previous fiscal years under paragraph seven exceeds NOK 5 million, the taxpayer may require deduction of net interest expenses carried forward and net interest expenses for the year within the limit provided for in this paragraph.

(4) An affiliated party pursuant to this section shall cover

a. any company or entity that, directly or indirectly, is at least 50 per cent owned or controlled by the borrower;

...

An individual, company or entity is considered to be an affiliated party pursuant to the third subsection if the requirement of ownership or control pursuant to the subsection has been met at some point in time in the course of the fiscal year.

8. Section 10-2 of the Norwegian Tax Act entitled “Deduction for group contributions” read, in extract:

(1) Private limited liability companies and public limited liability companies may claim a deduction in connection with income tax assessment for a group contribution to the extent that these are within the otherwise taxable general income, and to the extent the group contribution is otherwise lawful under the rules of the Private Limited Liability Companies Act (aksjeloven) and the Public Limited Liability Companies Act (allmennaksjeloven). Equivalent companies and associations may claim a deduction for a group contribution to the extent that private limited liability companies and public limited liability companies may do so. The second sentence of the first paragraph of Section 10-4 is nevertheless not applicable where a cooperative undertaking pays a group contribution to an undertaking that belongs to the same cooperative federation; see Section 32 of the Act relating to cooperatives (samvirkeloven).

...

9. Section 10-3 of the Norwegian Tax Act entitled "Tax liability for group contributions received" read, in extract:

(1) A group contribution constitutes taxable income for the recipient in the same fiscal year as it is deductible for the transferor. That part of the group contribution that the transferor may not deduct due to the rules in the second paragraph of Section 10-2 or because it exceeds the otherwise taxable general income, is not taxable for the recipient.

(2) A group contribution does not constitute a dividend for the purposes of Sections 10-10 to 10-13.

10. Section 10-4 of the Norwegian Tax Act entitled "Conditions for entitlement to make and receive group contributions" read, in extract:

(1) The transferor and the recipient must be Norwegian companies or associations. Private limited liability companies and public limited companies must belong to the same group, see Section 1-3 of the Private Limited Liability Companies Act and Section 1-3 of the Public Limited Liability Companies Act, and the parent company must own more than nine-tenths of the shares in the subsidiary and have a corresponding part of the votes that can be given in general meetings, see Section 4-26 of the Private Limited Liability Companies Act and Section 4-25 of the Public Limited Liability Companies Act. These requirements must be fulfilled at the end of the fiscal year. A group contribution may be made between companies domiciled in Norway even though the parent company is domiciled in another State, provided that the companies otherwise fulfil the requirements.

(2) A foreign company domiciled in a country within the EEA is considered equivalent to a Norwegian company provided that:

(a) the foreign company corresponds to a Norwegian company or association as referred to in the first paragraph of Section 10-2;

(b) the company is liable to taxation pursuant to point b of the first paragraph of Section 2-3 or Section 2 of the Petroleum Act, read in conjunction with Section 1; and

(c) the group contribution received constitutes taxable income in Norway for the recipient.

…

III Facts and procedure

11. PRA Group is a global group engaged in the acquisition of financial assets and debt servicing. The group has several companies in Europe, which are owned by the holding company PRA Group Europe Holding S.à.r.l., the latter being subject to taxation in Luxembourg. PRA Group Europe Subholding AS was a wholly-owned subsidiary of PRA Group Europe Holding S.à.r.l. and subject to taxation in Norway.

12. PRA Group Europe Subholding AS was financed with a combination of equity and loan capital from PRA Group Europe Holding S.à.r.l. The interest expenses for the Norwegian fiscal years 2014 and 2015 are related to that debt. PRA Group Europe Subholding AS did not receive any other value transfers from the parent company in 2014 and 2015.

13. In its tax returns for 2014 and 2015, PRA Group Europe Subholding AS claimed a deduction for that debt interest. In the tax assessments interest deductions amounting to a total of NOK 144 549 153 for the fiscal years 2014 and 2015 were disallowed on grounds of Section 6-41 of the Norwegian Tax Act. Under Section 6-41(3) of the Norwegian Tax Act, in relation to the deduction of interest paid on debt owed to affiliated parties, the debtor may not deduct interest in excess of 30% of "general income or uncovered loss for the year before the limitation of deductions under this Section, plus interest expenses and tax depreciation, and less interest income" (the "EBITDA").

14. According to the referring court, in light of the relevant preparatory works, the purpose of Section 6-41 of the Norwegian Tax Act is to counteract tax adaptations whereby international groups place disproportionately large shares of a group's debt, and thus interest expenses, in countries with high tax rates, whilst interest income and financial assets are channelled to group companies domiciled in countries with lower, or no taxation.

15. By letter of 7 December 2016, and after PRA Group Europe Subholding AS had been merged into PRA, the latter requested the tax assessments for the fiscal years 2014 and 2015 to be amended.

16. Following a review on the merits, the Tax Office upheld the tax assessments for 2014 and 2015 by decision of 7 July 2017. PRA appealed that decision to the Tax Appeals Board. By decision of 24 June 2020, the Tax Appeals Board, sitting in extended composition, dismissed the appeal.

17. On 8 September 2020, PRA lodged proceedings before Oslo District Court, seeking to be allowed a full tax deduction for interest payments on debt owed to affiliated companies. The Norwegian Government, represented by the Tax Administration, contends that the claim should be dismissed.

18. PRA claims that the limited interest deduction rule is contrary to the freedom of establishment provided for in Article 31 EEA, and that Norway is under an obligation to allow a full deduction for debt interest accrued. PRA contends that, for the determination of whether the limited interest deduction rule in Section 6-41 of the Norwegian Tax Act is contrary to the EEA Agreement, the Norwegian rules on group contributions in Sections 10-2 to 10-4 of the Norwegian Tax Act are relevant. Group contributions are value transfers between companies or associations in a group which, subject to certain conditions, allow the transferor to claim a tax deduction. The contribution is then deemed to be taxable income for the recipient. It may consist of an immediate transfer of funds or other assets, or that the transferor undertakes to pay a specified amount to the recipient at a later time.

19. According to the referring court, the provisions on group contributions are intended to support taxation neutrality between undertakings that organise their business operations through departments in a limited liability company and undertakings that organise their operations through several limited liability companies, in a group. Section 10-4(1) and (2) of the Norwegian Tax Act provides that only companies that are liable to taxation in Norway may make or receive group contributions with tax effects. It follows from the request that, as a group contribution with tax effect forms part of the basis for the calculation of the EBITDA, the recipient of a taxable group contribution will then have increased its maximum tax deduction for debt interest, whilst the transferor will have an equivalent reduction.

20. In the course of the proceedings before Oslo District Court, reference was made to a reasoned opinion (Decision No 192/16/COL) issued by the EFTA Surveillance Authority ("ESA") on 25 October 2016. The background to this reasoned opinion is as follows.

21. In 2014, ESA received a complaint concerning the operation of Section 6-41 of the Norwegian Tax Act, which entered into force on 1 January 2014. Following a review of the rules and an exchange of views with the Norwegian Government, ESA adopted a reasoned opinion on 25 October 2016. ESA concluded that, by maintaining in force rules on interest deductibility restrictions, such as those laid down in Section 6-41 of the Norwegian Tax Act, Norway had failed to fulfil its obligations under Article 31 EEA. ESA took account of the fact that groups of companies with Norwegian group members would more readily be able to avoid the operation of the interest limitation rules due to their ability to apply and benefit from the Norwegian group contribution rules. This

could deter Norwegian companies from establishing cross-border groups with affiliated group members in other EEA States and *vice versa*. ESA considered that the measures were not proportionate to any stated overriding reason in the public interest and could not therefore be justified.

22. While the Norwegian Government did not agree with the position adopted by ESA in its reasoned opinion, it indicated that it would propose further amendments to the interest limitation rules. These amendments, which inter alia introduced certain exceptions to the rules restricting interest deductions, entered into force on 1 January 2019. According to ESA, the assessment of the amended legislation is still ongoing.

23. Oslo District Court decided to stay the proceedings and by letter of 1 July 2021, registered at the Court on the following day, submitted the following questions to the Court:

> **1. Is there a restriction within the meaning of Article 31 EEA, read in conjunction with Article 34, when group contributions from Norwegian companies increase the maximum deduction for interest and thus the entitlement to deduction of interests on debt to affiliated parties under the limited interest deduction rule, a possibility which, under Norwegian tax rules, is not available for investments by or in EEA companies?**
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> **2. Is an EEA company that is in a group with a Norwegian company in a comparable situation to that of a Norwegian company that is in a group with another Norwegian company, and what significance does it have for the comparability assessment that no actual group contribution has been made from the EEA company to the Norwegian company, but rather a loan?**
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> **3. In the event that there is a restriction: Which reasons in the public interest may justify such a restriction?**

IV Written observations

24. Pursuant to Article 20 of the Statute of the Court and Article 90(1) of the Rules of Procedure, written observations have been received from:

- PRA Group Europe AS, represented by Anette Fjeld, advocate;
- the Norwegian Government, represented by Ida Thue, acting as Agent;
- ESA, represented by Claire Simpson, Kyrre Isaksen and Melpo-Menie Joséphidès, acting as Agents; and
- the European Commission ("the Commission"), represented by Wim Roels and Vincent Uher, acting as Agents.

V Proposed answers submitted

PRA

25. PRA submits that the questions referred should be answered as follows:

Question 1:

There is a restriction within the meaning of Article 31 EEA, read in conjunction with Article 34, when group contributions from Norwegian companies increase the maximum deduction for interest and thus the entitlement to deduction of interests on debt to affiliated parties under the limited interest deduction rule, a possibility which, under Norwegian tax rules, is not available for investments by or in EEA companies.

Question 2:

An EEA company that is in a group with a Norwegian company is in a comparable situation to that of a Norwegian company that is in a group with another Norwegian company. It is without significance for the comparability assessment that no actual group contribution has been made from the EEA company to the Norwegian company.

Question 3:

In the event that there is a restriction, the restriction cannot be justified by overriding reasons in the public interest.

The Norwegian Government

26. The Norwegian Government proposes that the questions referred be answered as follows:

Questions 1 and 2:

National provisions on interest limitation and group contribution, such as those at issue in the main proceedings, do not constitute a restriction under Article 31 EEA.

Question 3:

Article 31 EEA does not preclude national provisions on interest limitation and group contribution, such as those at issue in the main proceedings.

ESA

27. ESA proposes that the questions referred be answered as follows:

Question 1:

Articles 31 and 34 EEA must be interpreted as meaning that national legislation, such as that at issue in the main proceedings, will restrict the freedom of establishment where a company liable to taxation in Norway may, by using group contribution rules, lessen or remove the impact of rules limiting interest deductions in respect of loans taken out with affiliated companies, provided it is in a group with other companies liable to taxation in Norway, whereas this is not possible if it is in a group with companies liable to taxation in other EEA States.

Question 2:

In the context of such national legislation, an EEA company which is in a group with a Norwegian company is in a comparable situation to that of a Norwegian company which is in a group with another Norwegian company. It is not significant for the comparability assessment that, under the national legislation, the EEA company is unable to make a group contribution to the Norwegian company.

Question 3:

Such national legislation may be justified where it serves the legitimate objective of preventing wholly artificial arrangements leading to tax avoidance. However, the requirements of national law go beyond what is necessary to pursue such an objective.

The Commission

28. The Commission submits that the questions referred should be answered together as follows:

> *Article 31 EEA, read in conjunction with Article 34, must be interpreted as not precluding national legislation, such as that at issue in the main proceeding, pursuant to which group contributions from domestic companies increase the interest deduction cap set at 30% of tax EBITDA and thus the entitlement to deduction of interests on debt to affiliated parties, a possibility which, under national tax rules, is not available for investments by or in EEA companies.*

Bernd Hammermann
Judge-Rapporteur