

D V. INSPECTOR OF TAXES

By Philip Baker QC

C – the Second Question Referred for a Preliminary Ruling

1. A rhetorical question

[72] The solution proposed to the first question referred for preliminary ruling renders it superfluous to respond to the second. Nevertheless, let me be permitted to make certain subsidiary comments in case the Court of Justice follows a different course.

[73] The referring court asks whether the conclusion that the tax regime introduced by the “BV Law” does not violate Article 56 of the EC Treaty might be reconsidered in the light of the double taxation convention concluded between the Netherlands and Belgium, which extends to persons resident in the latter Member State who own immovable property in the first State the tax advantages granted by the Netherlands legislation to its own residents, in cases where the relief provided for these latter residents is applicable.

[74] The question is based on the premise that the first question referred for a preliminary ruling has received a negative answer because, in order to reach a decision on the question of equality in respect of freedom of movement of capital, the Court of Justice would have considered that, with regard to taxes on

capital in the Netherlands, the situation of a German resident is not comparable to that of a Dutch resident, even if they both own capital in that Member State of an identical value which represents the totality of their taxable capital. Once that conclusion is reached, the second question for a preliminary ruling would be superfluous since there would be no possible comparison if the owners of these properties resided one in Germany and one in Belgium.

[75] However, if one considers that the situation at issue in the main litigation (that of D and that of a taxpayer living in the Netherlands) can be compared one to another, it would be equally necessary to put on the same plane the two situations to which this second question refers (that of D and that of a person taxable in the

Netherlands who resided in Belgium) and it would be necessary to analyse these from a strictly hypothetical and subsidiary view, without the results of this analysis entering in any way into the resolution of the decision which must be taken on the request for a reference.

[76] In 1998, according to the bi-lateral convention cited above, a Belgian resident having immovable property in the Netherlands benefited in this latter State from a tax treatment which was more advantageous than a German resident in the same situation, because he had the right to a relief to which the latter was not entitled, while neither of these two paid any tax on their capital in their country of origin. As a result of this international accord, the Netherlands legal system discouraged Germans from investing their savings in the Netherlands, if one compared them to persons residing in Belgium.

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[77] To determine whether this situation can be permitted by Community law, one has to consider the meaning of Article 293 of the EC Treaty.

2. The competence of Member States to relieve double taxation within the Community by the conclusion of bi-lateral agreements

[78] The elimination of the phenomenon of double taxation is an objective of the Treaty¹, intimately linked to the establishment of the internal market².

[79] Nevertheless, as the Court of Justice noted in the Gilly case, it should be noted that to the present day, with the exception of the Convention of the 23rd July 1990 relating to the elimination of double taxation on the adjustment of profits of associated enterprises³, no measure of unification or harmonisation aimed at the elimination of double taxation has been adopted in the Community Legal Order.

[80] Article 293 of the EC Treaty authorises Member States to enter into negotiations for this purpose⁴. In the absence of a multi-lateral treaty signed by all the partners of the Community, bi-lateral conventions have been concluded

¹ In its judgment of the 11th July 1985, Mutsch (137/84, Rec. p.2681) at point 11 the Court of Justice declared that Article 220 of the EC Treaty required Member States to extend to residents of other Member States the guarantees which it grants to its own residents. In the judgment of the 12th May 1998, Gilly (C-336/96, Rec. p.I-2793), at point 16, it is stated more precisely that “the elimination of double taxation within the Community figures ... amongst the objectives of the Treaty.”

² As the former judge of the Court, Melchior Wathelet, wrote with the clarity and

conciseness which characterises him, in “Double Taxation Conventions in the Jurisprudence of the Court”, his contribution to the collection of essays in honour of Gil Carlos Rodriguez Eglisas “Une Communauté de Droit” (Berliner Wissenschafts-Verlag, 2003), p.445.

³JO L 225, p.10.

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by those who have decided to act together to restrict their tax sovereignty by renouncing a part of it. In other words, these treaties have as their object the allocation of the power to set the criteria for imposing tax on the tax base. [81] The exercise of this power can give rise to differences, taking account of the fact that there is no harmonisation of national tax rules.

[82] But, to be legitimate, the exercise of the power must respect the limits which are assigned to it, any over-stepping [of those limits] being unjustified. On the other hand, as I have observed, the competence of Member States to sign bi-lateral agreements, as in this case, has as its object the allocation of taxing power such that, where there is nothing to allocate, the agreement has no purpose. As taxation on capital did not exist in Belgium, Article 25(3) of the Treaty with the Netherlands⁶ - to the extent that it extends to Belgian residents the benefit of the relief granted to Dutch residents – becomes purely and simply a privilege without counterparty or reciprocity such that the examination of its “Communityness” [*communautarité*] must be particularly exacting. The arguments and the consequences – to which I will refer below – put forward, with a certain alarmism, by the governments which submitted observations, disappear like a column of smoke because the legal rule in question has nothing

⁴In the conclusions presented on the 20th November 1997 in the Gilly case, I pointed out that this provision leaves a large margin of appreciation to Member States to decide whether or not it is necessary to enter into negotiations (point 35).

⁵The Court expressly recognised this at point 30 in the Gilly case.

⁶The OECD Model Convention contains no equivalent provision.

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to do with the specific contents of agreements which try to eliminate international double taxation.

[83] As a consequence, the difference of treatment created by the Dutch tax system, of which the treaty cited above is an integral part, between taxpayers residing in Belgium and those residing in Germany, is incompatible with Articles 56 and 58 to the extent that it renders more difficult the free movement of capital between this latter Member State and the Netherlands.

[84] Even if one considered that a national tax regime like that under consideration is the result of a strict application of the fiscal power to prevent double taxation, its

conformity with Community law would not necessarily be assured. In this context, it is necessary to refer once again to the Court's case law.

3. The case law of the Court of Justice on the exercise by Member States of the competence granted by Article 293 of the EC Treaty

[85] As I have emphasised, Member States may freely exercise their fiscal sovereignty, but on condition they respect Community law both in their individual actions and when they act in concert⁷. The invitation made in the provision of the Treaty cited above must not lead to a result contrary to that which is desired, which is the creation of a single market by the

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implementation of the fundamental freedoms of movement, since the fact that a taxable subject is liable to be taxed twice constitutes the most serious obstacle to the crossing of internal frontiers by persons and by their capital.

[86] Each time the Court of Justice has analysed the contents of this kind of bilateral convention, the reference point has always been a person who, while residing in one of the two Member States concerned, complained of the fact that the application of the convention made him subject to discrimination in the other State. The Gilly case concerned the amount of individual income tax payable in Germany by a couple living in France, in accordance with the rules of the convention of 21st July 1959 between these two States. For its part, the judgment of the 12th December 2002⁸, *De Groot*, dealt with the situation of a Dutch resident who, for the tax year 1994, worked as a salaried employee for companies of the same group in the Netherlands and in three other Member States (Germany, France and the UK) which had each concluded a double taxation convention with the Netherlands.

[87] The panorama changes however when it is a matter of legal persons. In the case of *Metallgesellschaft*, cited above, the question was posed whether the authorities of one Member State could refuse to a company of another Member State a tax credit granted to resident companies and to those established in Member States with which that State had concluded double taxation

⁷The Court of Justice has constantly maintained this stance since its judgment of the 28th January 1986, *Commission v. France* (270/83, case known under the name of “*Avoir fiscal*”, Rec. p.273) at point 26.

⁸Judgment of the 12th December 2002, *De Groot* (C-385/00, Rec. p. I-11819).

conventions. In fact, the Court referring the question wished to know whether by means of treaties of this kind, it was possible to introduce differences between companies of the various Community States. Unfortunately, the Court of Justice did not find it necessary to respond to this point (point 97).

[88] A similar issue arose in the case of Saint-Gobain ZN – to which I have also referred – since in that case, a permanent establishment in Germany of an enterprise resident in another Member State sought to benefit in Germany from advantages - in respect of the taxation of dividends received from companies established in third countries not members of the Community (the Swiss Confederation and the USA) - granted to local companies by the double taxation conventions concluded with these countries.

[89] As one can see, these two cases have a certain similarity with the case of D who claims in the Netherlands the same treatment to that accorded, by virtue of a bi-lateral agreement, to Belgian residents. The Court of Justice should, therefore, on the basis of this triangular relationship and by comparison with the foreign elements (Germany and Belgium) grant a satisfactory response from the point of view of the requirements of Community law.

4. The non-discrimination principle and the most favoured nation clause

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[90] The governments which presented observations in this case and the Commission were unanimously opposed to the Court - on the basis of the above-mentioned treaty - reaching an interpretation of Article 56 in the sense that residents of Germany and the Netherlands could benefit from the same treatment as Belgian residents.

[91] In particular, the Dutch Government explained in detail the differences between the present case and the facts which led to the decisions in the Saint-Gobain ZN case, cited above, and the Gottardo case⁹ in both of which a Member State had within its jurisdiction nationals of other Community States and where it was necessary to determine if it was obliged to extend to them the benefits granted to local residents by virtue of international conventions entered into with third countries. In reality, this latter fact is the sole difference since one is concerned in this case with a bi-lateral agreement with another Member State. On all other points, the situations are identical.

[92] Madame Gottardo, of Italian origin but with French nationality by marriage, wanted the amount of her retirement pension to be fixed in her country of birth, by taking account not only the contribution periods in these two States, but also of

those spent in Switzerland, in conformity with an Italian-Swiss social security convention which, in fixing the amount of the pension, granted to Italians the right to take into account the time spent

9 Judgment of the 15th January 2002, Gottardo (C-550/00, Rec. p. I-413) which dealt with a bi-lateral social security convention concluded with a third country. In that case, the Court of Justice followed my conclusions of the 5th April 2001.

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working in the Swiss Confederation. The case of Saint-Gobain ZN concerned a company established in France which, having paid tax in Germany on the profits and on the capital of a branch situated on German territory, sought to benefit from the tax advantages granted to companies domiciled in Germany, in conformity with both the double taxation convention entered into with Switzerland and the double taxation convention entered into with the United States. D is a German resident taxable in the Netherlands on immovable property which he owns in that country; he wants to benefit from the tax benefit granted by the legal system of this Member State to Belgian residents owning immovable property in the Netherlands, in accordance with the agreement concluded with this latter country. The only difference between those cases and the present case exists in the fact that, in the former cases, the convention was entered into with a third country not a member of the Community.

[93] This difference is not, however, sufficient to reach a different solution.

[94] In fact, the convention with which this case is concerned is distinguished from those considered in the Saint-Gobain and Gottardo cases in that it falls plainly within the scope of application of the Treaty (Article 293 of the EC Treaty) such that any risk that its literal interpretation would present an obstacle to the application of a Community provision requires Member States, even more so than in the cases cited, to do what is necessary to avoid this result. It may seem superfluous, but the observations presented by the

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governments participating in the hearing lead me to recall that when Member States exercise their fiscal competence, they must respect Community law whatever the normative instrument used - law, regulation or international convention, whether intra-community or with a third country. That is why, in the Gottardo case, the Court of Justice declared that “in implementing obligations which are undertaken by virtue of international conventions, *whether it concerns a convention between Member States or a convention between a Member State and one or more third countries*¹⁰, Member States must, subject to the exceptions in Article 307 EC, respect the obligations imposed on them by virtue of Community

law” (point 33).

[95] Consequently, in comparing the situation of D to that of a Belgian resident with regard to the payment in the Netherlands of tax on their respective immovable property, the former [D] is entitled to the benefits which the double taxation convention entered into between these two States grants to the latter, since the non-application of that convention is such that it would create an unjustifiable obstacle to the free movement of capital.

[96] Like the governments which participated in the hearing, I consider that the most favoured nation clause cannot be automatically transposed to the realm under consideration here or, to put it another way, the non-discrimination principle on grounds of nationality, as a rule applicable to freedom of movement, does not require that a citizen of a Member State receives in

¹⁰ My italics.

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another Member State the best treatment possible, regardless of whether or not this is necessary for the construction of a single market. The same point of view underpins the considerations which I developed at points 66 and 67 of my Opinion in the Gilly case, where I declared with regard to income tax on individuals that the object of a bi-lateral double taxation convention is to ensure that income already taxed in one Member State should not be taxed again in the other, and not to guarantee to the taxpayer the most favoured tax status in each possible case.

[97] But nothing prevents Community law from offering a solution to end a situation of inequality¹¹ when the application of a rule in a treaty by a Member State presents an obstacle to the free movement of capital by the application in an unjustified manner of a different treatment to persons resident in other Member States (to whom Article 12, first paragraph, EC gives the right – by virtue of their status as European citizens – not to be discriminated against, directly or indirectly, by reason of their nationality). In other words, in triangular situations like that in the main litigation, the position of the taxpayer in the taxing State may be constructed on the basis of the most favoured nation clause, but equally on the basis of the existence of a restriction to the freedoms of movement. In effect, the taxpayer may attempt, as does D, to obtain the

¹¹ Thus, the Court has underlined on many occasions, to the point that it has become superfluous to cite it, that Article 12 of the EC Treaty can only be applied in an autonomous manner in situations regulated by Community law for which the Treaty does not provide any specific non-discrimination rules. Thus, by contrast with the freedom of movement of workers (article 39(2) EC Treaty), freedom of establishment (article 43, first paragraph, EC Treaty) and the freedom to supply services (article 49, first paragraph, EC Treaty), the free movement of capital has no particular norm of this type (article 56,

EC Treaty); in that case, the only reference to discrimination is that which, in article 58(3) EC Treaty,

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extension to him of the benefit of the agreement which is provided for Belgian residents, and this contention may draw upon the concept of restriction to the free movement of capital if the heavier tax charge and the negative consequences are considered to be contrary to the Community Legal Order. In summary, it is contrary to Community law to accept reciprocal obligations with respect to another Member State when these limit the freedoms of movement of nationals of third European States¹². It should not be forgotten that national rules, of which international treaties lawfully concluded and ratified form part, cannot violate the fundamental freedoms of the European legal system.

limits the power to adopt certain measures recognised by paragraph 1, and since, by its scope, it includes all forms of unjustified discrimination including that targeted by Article 12, EC Treaty.

[98] The governments which have submitted their observations in the present case are most definitely opposed to the above statements for various reasons.

[99] They maintain the impossibility of comparing the situation of D with that of a taxpayer resident in Belgium; the conventions concluded within the scope of Article 293 EC Treaty are the product of negotiations which take into account the structures and the contents of the respective fiscal systems such that to conclude that a concrete tax situation is identical it would be necessary to take into account not simply an isolated provision or even the entirety of the convention, but the whole of the national fiscal system. As the Commission has

¹² See FA Garcia Prats, “*Convenios de doble imposición, establecimientos permanentes et derecho comunitario (Consideraciones en torno a los casos Royal Bank of Scotland et Saint-Gobain)*”, Noticias de la Unión Europea, no. 191, December 2000, pp. 9 – 54, particularly p. 49.

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emphasised in very clear terms, the different treaty regimes create different situations, which are not comparable.

[100] If it had been accepted, this maximalist point of view above would have prevented the adoption of the judgments in *Gottardo* and *Saint-Gobain ZN*, as well as all forms of test having as their object the verification of the existence of a situation of equality; in effect, if – apart from the similarity in facts and applicable norms – it was necessary to establish a similarity between the rationale for the norms, their basis, the procedure followed to adopt them and the legal structure into which they are inserted, no situation of equality could ever be identified and there would never, or virtually never, be comparable situations. In reality, the examination of the question of equality is simpler and more modest, since it

requires the determination of whether two individuals in comparable factual situations are subject without justification to different rules; in the context of the examination of these rules, the only relevant point is to see if their application produces different effects, to the disadvantage of one or other of these individuals.

[101] I am well aware of the risks which the above considerations pose for the equilibrium and the reciprocity which governs the regime of conventions for the avoidance of double taxation, but these inconveniences should not constitute obstacles to the construction of a single market. On the one hand, in fixing in these agreements criteria for taxation which permit the allocation of fiscal competence, Member States must act with more prudence and avoid

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provisions liable to impede the realisation of this objective. On the other hand, the right to equal treatment has its own autonomous character with regard to reciprocity such that in cases of conflict it takes priority over mutual undertakings. If the bi-lateral exchange of obligations contained in a convention of this type conflicts with the fundamental ideas which propel the construction of a united Europe, the States affected are required to search for other formulae to achieve their objective without prejudicing citizens of other Member States in violation of the Community Legal Order. This is what the principle of proportionality requires. [102] The British Government argued that the most favoured nation status creates a risk of tax avoidance since a taxpayer could invoke the least severe anti-avoidance provisions included by a Member State in its conventions concluded with other States.

[103] But this argument lacks substance. In the first place, it is not a matter of the application of the principle of the most favourable national treatment, but of the effectiveness of the fundamental rules of Community law which may at times lead to similar results to those produced by this principle. Secondly, the alleged risk is purely hypothetical in the circumstances of the main proceedings, since D does not ask to be exempted from fiscal controls, but asks for a concrete and precise tax advantage.

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[104] Finally, if the fight against tax avoidance was raised to an absolute rule of public interest to justify restrictions to the freedoms of movement, one would have to discuss the possibility of subjecting intra-community movements of capital to a regime of prior authorisation. In my opinion in the matter which gave rise to the case of *Commission v. France* cited above, I underlined (at point 27) that the fight

against tax avoidance is not a blank cheque given to Member States to pare down the freedoms; on the contrary, like all exceptions to the cardinal principles of the construction of the Community, it must be interpreted and applied having regard to the requirements of the principle of proportionality. Thus, difficulties in the work of managing and assessing taxes are not sufficient to justify imposing restrictions of an absolute character on fundamental freedoms while ignoring other less expedient, but equally less restrictive, means which would permit the attainment of the same objective.

[105] A positive response to the second question for a preliminary ruling would have a significant impact on the complex network of bi-lateral double taxation conventions entered into within the Community, but this would not be the first time that a decision of the Court impacts on the legal regime of the Member States.

[106] Consequently, having regard to the subsidiary character of this second question for preliminary ruling and to the answer given to the first question, I

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propose to the Court not to answer it or, in any case, to respond in accordance with the guidance set out in the above paragraphs.