

FISCAL NEUTRALITY AND EU LAW*

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Introduction

The objective of this article is to investigate whether the principle of fiscal neutrality is a general principle of EU law. This principle was discussed by Professor Wolfgang Schön in the Bulletin for International Taxation (May/June 2015) entitled: “*Neutrality and Territoriality – Competing or Converging Concepts in European Tax Law*.”²

Schön argued that the internal market is rooted in the same “efficiency-oriented thinking as the concept of tax neutrality”. He bases much of his reasoning on a reading of Article 120 TFEU and Article 121(1) TFEU, on the objectives of the EU as set out in Article 3 TEU and on the wording and interpretation given to the fundamental freedoms in the Court’s jurisprudence, in particular, the Court’s restriction analysis terminology of “deter”, “discourage” and “dissuade”.

Schön suggests that fiscal neutrality is a “concept of EU law”.³ In support of his argument, he highlights the prohibition of internal customs duties on import and export and all charges of equivalent effect under Article 30 TFEU and the fact that this provision is complemented by Article 110 TFEU.

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2 Bulletin for International Taxation, April/May 2015, 271-293.

3 Whilst it is certainly a concept of EU law in relation to certain EU rules, it will be shown in this article that it does not constitute a general principle of EU law.

Schön points out that “the ECJ has made it clear over the last 30 years that any legislation in the area of direct taxation that results in the unequal treatment of cross-border activities as opposed to purely domestic activities is forbidden, unless the Member State can demonstrate a valid justification for that legislation”. He argues that the Court’s direct tax jurisprudence has evolved from a limited concept of discrimination of persons on grounds of nationality to a simple and far reaching prohibition on cross-border tax obstacles to economic entities and transactions in general.⁴

Schön suggests that the unilateral neutrality test clarifies that “the non-discrimination principle is not intended to place the ‘international’ taxpayer in a more beneficial position than the treatment of a taxpayer in a purely domestic situation”.⁵

In his analysis of the direct tax jurisprudence of the CJEU, Professor Schön highlights numerous instances of inconsistency with the principle of fiscal neutrality. Yet, at no stage does he question whether the principle of neutrality is actually in operation when a fundamental freedom is exercised.

4 An alternative view is that the non-discrimination principle and the abolition of restrictions on the exercise of the fundamental freedoms are contained in the Treaty of Rome and in the current Treaty on the Functioning of the European Union. They have changed little since 1957. The Court has merely interpreted these principles based on the cases that have been brought before it via the preliminary ruling procedure or by the European Commission bringing infringement proceedings before the Court. The Court has made it clear in its jurisprudence that all discrimination – direct and indirect – constitutes a restriction on the exercise of a fundamental freedom that requires justification if it is to be maintained. However, the Court has also demonstrated in its case law that all restrictions are not necessarily discriminatory. This jurisprudence depends on the rules contained in the Treaties and the fact that the Court has accepted general interest justifications put forward by the Member States to justify maintaining their non-discriminatory, yet restrictive, direct tax rules.

5 The non-discrimination principle works somewhat differently to that suggested by Schön. The principle of equal treatment tries to ensure that the person who is exercising a fundamental freedom in a host Member State context, usually a foreigner, is treated no less favourably in that State than a host Member State national. From an origin Member State perspective, the principle of equal treatment tries to ensure that an origin Member State national, exercising a fundamental freedom right, is treated no less favourably than another origin Member State national. In relation to the free movement of workers, the Court has held that two non-resident workers who come to the host Member State to work may have to receive equal treatment in the host Member State. See *C.G. Sopora v Staatssecretaris van Financiën* (“*Sopora*”), C-512/13, ECLI:EU:C:2015:108. The Court’s current view is that the non-discrimination principle does not prevent reverse discrimination. Thus, in *Van Hilten*, Dutch inheritance tax rules that treated Dutch nationals worse than foreigners were accepted by the Court. See *Heirs of M.E.A. van Hilten-van der Heijden v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen* (“*Van Hilten*”), C-513/03, ECLI:EU:C:2006:131. Similarly, in *Bouanich I*, Mrs Bouanich could have been treated better under the Swedish-French double tax convention than a Swedish resident making a similar investment in the same Swedish company. See *Margaretha Bouanich v Skatteverket* (“*Bouanich I*”), C-265/04, ECLI:EU:C:2006:51. Therefore, the equal treatment principle requires no less favourable tax treatment rather than the unilateral fiscal neutrality suggested by Schön.

Schön highlights that the Member States do not apply worldwide taxation to residents and non-residents and that generally, residents and non-residents are not comparable. He notes that this represents “a major deviation from the concept of cross-border neutrality as ensured by the fundamental freedoms.” He points out that this appears to undermine fundamentally, “the effect of the principle of non-discrimination⁶ in tax cases, but also ... explicitly requests a different treatment of residents and non-residents in a generalised fashion ... This blunt concept of non-comparability is clearly overreaching”.⁷

Schön states that the concept of tax neutrality, which requires domestic tax laws to be judged on a stand-alone basis, “results in the conclusion that the Member States cannot be forced to take into account taxes paid to foreign jurisdictions ... He points out that a “true one-dimensional, non-discrimination test of Member States’ legislation...must regard the legislation of the other Member States to be non-existent”.⁸

Schön suggests that the Court “created implicitly an order with regard to taxation of corporate profits. The tax on the corporate profits belongs to the source Member State and the tax on the dividend belongs to the residence Member State.⁹ Only if the source Member State grants relief for underlying corporate income tax is the residence Member State redeemed from its obligations”.

In relation to *Schumacker*, Professor Schön submits that “a unilateral view on tax neutrality would simply require each Member State to apply its domestic rules on

6 Schön fails to accept the definition of discrimination in EU law which states that discrimination can arise only through the application of different rules to comparable situations or the application of the same rule to different situations. See *Finanzamt Köln-Altstadt v Roland Schumacker* (“*Schumacker*”), C-279/93, ECLI:EU:C:1995:31, para. 30. This definition of discrimination has been used by the Court from the outset. See, for example, *Italian Republic v European Commission* (“*Refrigerators*”), C-13/63, ECLI:EU:C:1963:20, part 4(a).

7 The Court’s approach to the different treatment of residents and non-residents in a direct tax environment was clearly set out in *Schumacker* and explained in more detail by Advocate General Philippe Léger in his Opinion in that case. This approach has been adopted by the Court since that judgment.

8 Schön fails to understand the role played by double tax conventions (DTCs) in the Court’s jurisprudence, in the absence of DTC rules at the EU level. DTCs form part of the legal background to many of the cross-border disputes in the Court’s case law. See, for example, *G. H. E. J. Wielockx v Inspecteur der Directe Belastingen* (“*Wielockx*”), C-80/94, ECLI:EU:C:1995:271, where the Court determined that the coherence of a national tax regime may be raised from the level of an individual taxpayer to the level of a DTC and *Margaretha Bouanich v Skatteverket* (“*Bouanich I*”), C-265/04, ECLI:EU:C:2006:51, where the Court accepted that a DTC formed part of the legal background to the case before it and, as such, the Court had to take it into account in order to give an interpretation of EU law that was relevant to the national court.

9 This is simply not correct. A source Member State may impose a withholding tax on an outbound dividend in a situation where it imposes a similar tax on a domestic dividend payment.

deductions and similar benefits in a non-discriminatory fashion to cross-border benefits. He points out that this is not what the ECJ has done since *Schumacker*.¹⁰ On the issue of cross-border loss relief, Schön argues that the “technique of making the availability of losses in one Member State dependent on the situation in the other Member State is incompatible with the principle of tax neutrality and the ongoing existence of double taxation and disparities”.¹¹

Schön argues that the Court’s jurisprudence concerning cross-border tax credits is not in line with tax neutrality and suggests that the Court went too far in *Manninen*. He submits that the Court “did not take note that that the cross-border imputation for the underlying corporate income tax is linked to the problem of double taxation in general. The concept of tax neutrality that requires domestic tax laws to be judged on a stand-alone basis results in the conclusion that the Member States cannot be forced to take into account taxes paid to foreign tax jurisdictions”. Schön’s arguments concerning *Manninen* are investigated in more detail below.

Schön’s analysis therefore raises a number of interesting research questions. The main question which this essay will attempt to answer is whether the principle of fiscal neutrality is a general principle of EU law and an actual goal of the EU’s Internal Market.

By analysing some of the issues raised in Professor Schön’s article, this article will demonstrate that the principle of fiscal neutrality is not a general principle of EU law and that the failure to understand this affects the proper understanding of the Court’s direct tax jurisprudence, in particular, the principle of equal treatment, which is the

10 The Court has been consistent in its approach since *Schumacker*. See the contrast case *Gschwind*, where Germany was not required to grant personal allowances to a Dutch resident because the Court determined that, unlike *Schumacker*, *Gschwind* was not in a comparable situation to a German resident worker because the *Gschwinds* had sufficient taxable income in the Netherlands to receive their personal allowances there. See *Frans Gschwind v Finanzamt Aachen-Außenstadt* (“*Gschwind*”), C-391/97, ECLI:EU:C:1999:409.

11 The principle of equal treatment, from an origin Member State perspective, requires the origin Member State to grant loss relief cross-border if it grants similar loss relief in a domestic setting, unless it can demonstrate that it has a general interest justification for not granting that relief cross-border. This might be the case if the loss relief could be obtained in the host Member State. The Court dealt with this issue for the first time in its *Marks & Spencer* judgment. See *Marks & Spencer v David Halsey (Inspector of Taxes)*, (“*Marks & Spencer*”), C-446/03, ECLI:EU:C:2005:763, in particular, paragraph 55 where the Court set out the “no-possibilities test”. The only reason the United Kingdom was obliged to grant group relief cross-border in this case was because it granted group relief domestically and its legislation constituted a restriction on the freedom of establishment. If it had not granted group relief domestically, then no restriction on the freedom of establishment would have existed and the United Kingdom would not have been obliged to grant group relief for cross-border losses. See Tom O’Shea, “*Marks and Spencer v Halsey (HM Inspector of Taxes): Restriction, Justification and Proportionality*”, [2006] 15(2) EC Tax Review 66-82.

key principle underlying the Court's direct tax jurisprudence involving the fundamental freedoms.¹²

This article is divided into four parts. In Part I, the question whether the principle of fiscal neutrality is a general principle of EU law is explored. In Part II, an attempt is made to respond to some of Professor Schön's criticisms of the Court's jurisprudence, in particular, an alternative view of the cases is offered, based on the principle of equal treatment. Part III investigates whether the principle of equal treatment applies in relation to all cross-border situations, in particular, disparity situations. Part IV examines whether the jurisprudence of the Court has evolved in the way suggested by Professor Schön or whether discrimination and restriction analyses existed from the outset and continue to co-exist in the jurisprudence of the CJEU. Part V provides some conclusions.

Part I

Is the principle of fiscal neutrality a general principle of EU Law?

The principle of fiscal neutrality features in the Court's tax jurisprudence¹³ and is usually found in cases involving Value Added Tax and "Internal Taxation" (Article 110 TFEU, formerly, Article 90 EC), however, it has rarely been mentioned in the Court's direct tax jurisprudence related to the exercise of the fundamental freedoms. This can be explained, perhaps, in a number of ways: first, the issue may not have been decided by the Court to date; second, the principle of fiscal neutrality may simply not be applicable in fundamental freedom situations or third, the principle may apply only in those situations where it is specifically referred to in the TFEU or in a Directive, such as in the value added tax sphere or in the Parent Subsidiary Directive.¹⁴

Value Added Tax

In the VAT field, the Court has made it clear that the principle of fiscal neutrality is a "fundamental principle of the common system of VAT" and that, in particular, it "precludes treating similar goods which are in competition with each other, differently for VAT purposes".¹⁵

12 See Tom O'Shea, *EU Tax Law and Double Tax Conventions* (Avoir Fiscal, London, 2008) ISBN 9780955916403.

13 As such, it is definitely a "concept of EU law" as argued by Schön.

14 See Council Directive 90/435/EEC (as amended). See – https://ec.europa.eu/taxation_customs/business/company-tax/parent-companies-their-subsidiaries-eu-union_en (last visited 20 Jan. 2019)

15 *Marks & Spencer plc v Commissioners of Customs & Excise* ("M+S"), C-309/06, ECLI:EU:C:2008:211, para. 47.

The Court explained that the principle of fiscal neutrality “is the reflection, in matters related to VAT, of the principle of equal treatment”.¹⁶ However, the Court highlighted that the principle of fiscal neutrality was a more limited principle than the principle of equal treatment since an infringement of the principle of fiscal neutrality could occur only in relation to competing traders but an “infringement of the general principle of equal treatment may be established, in matters relating to tax, by other kinds of discrimination which affect traders who are not necessarily in competition with each other but who are nevertheless in a similar situation in other respects”.¹⁷

The Court noted in *Investrand* that common system of VAT “ensures complete neutrality of taxation of all economic activities, whatever their purpose or results, provided that they are themselves subject in principle to VAT”.¹⁸

In *NCC Construction Danmark*, the Court provided further important guidance on the principle of fiscal neutrality, confirming that the principle reflected, in matters of VAT, the general principle of equal treatment.¹⁹ However, the Court stressed that the principle of equal treatment was a general principle of EU law and has “constitutional status”,²⁰ whereas “the principle of fiscal neutrality requires legislation to be drafted and enacted, which requires a measure of secondary Community law”.²¹

The Court pointed out that “the general principle of equal treatment, of which the principle of fiscal neutrality is a particular expression at the level of secondary Community law and in the specific area of taxation, requires similar situations not to be treated differently unless differentiation is objectively justified”.²²

The Court concluded that in implementing the VAT Directive, “the Member States were obliged to take into account the principle of equal treatment, like the other general principles of Community law, which having constitutional status, bind those Member States when they take action in the field of Community law”.²³

From this VAT jurisprudence, it is evident that the principle of fiscal neutrality is not a general principle of EU law, but merely a reflection of the principle of equal

16 *M+S*, para. 49.

17 *M+S*, para. 49.

18 *Investrand BV v Staatssecretaris van Financiën* (“*Investrand*”), C-435/05, ECLI:EU:C:2007:87, para. 22.

19 *NCC Construction Danmark A/S v Skatteministeriet* (“*NCC Construction Danmark*”), C-174/08, ECLI:EU:C:2009:669, para. 41.

20 *NCC Construction Danmark*, para. 42.

21 *NCC Construction Danmark*, para. 42.

22 *NCC Construction Danmark*, para. 44.

23 *NCC Construction Danmark*, para. 45.

treatment in the area of VAT. It relies on the adoption of secondary EU legislation for its existence.

Thus, Council Directive 2006/112/EC of the 28th November 2006 on the common system of value added tax provided, in the Preamble, that a VAT system “achieves the highest degree of simplicity and of neutrality when the tax is levied in as general a manner as possible and when its scope covers all stages of production and distribution, as well as the supply of services”.²⁴

Recital (7) provides that “the common system of VAT should, even if rates and exemptions are not fully harmonised, result in neutrality in competition, such that within the territory of each Member State similar goods and services bear the same tax burden, whatever the length of the production and distribution chain”.

Finally, Recital (30) establishes that “in order to preserve neutrality of VAT, the rates applied by Member States should be such as to enable, as a general rule, deduction of the VAT applied at the preceding stage”.

The Preamble to the 2006 ‘Recast’ VAT Directive, therefore, includes the principle of fiscal neutrality as a fundamental component of the VAT regime.

Parent Subsidiary Directive

The Court applies similar reasoning in its jurisprudence concerning the Parent Subsidiary Directive.²⁵

In *Epson*,²⁶ the Commission noted that “the aim of the Directive is, in accordance with the principle of fiscal neutrality, to obviate double taxation in dealings between a parent company and its subsidiary where they are established in different Member States”.²⁷

24 Council Directive 2006/112/EC of the 28th November 2006 on the common system of value added tax Preamble Recital (5). See –

https://ec.europa.eu/taxation_customs/business/vat/existing-eu-legal-framework_en (last visited 20 Jan. 2019).

25 Council Directive 90/435/EEC of 23 July 1990 as amended. See - https://ec.europa.eu/taxation_customs/business/company-tax/parent-companies-their-subsidiaries-eu-union_en (last visited 22 Jan. 2019).

26 *Ministério Público and Fazenda Pública v Epson Europe BV* (“Epson”), C-375/98, ECLI:EU:C:2000:302.

27 *Epson*, para. 17.

Similarly, in *Banque Fédérative du Crédit Mutuel*,²⁸ the Court indicated that the Parent Subsidiary Directive sought “to ensure the neutrality, from the tax point of view, of the distribution of profits by a subsidiary established in one Member State to its parent company established in another Member State”.²⁹

To that end, the Court highlighted that “Article 4(1) of Directive 90/435 provides that, where a parent company, by virtue of its association with its subsidiary, receives distributed profits, the Member State in which the parent company is established must either refrain from taxing such profits or authorise the parent company to deduct from the amount of tax payable that fraction of the corporation tax paid by the subsidiary which relates to those profits and if appropriate, the amount of the withholding tax levied by the Member State in which the subsidiary is resident, up to the limit of the amount of the corresponding domestic tax”.³⁰

Mergers Directive

In the *A.T.* case,³¹ the Court dealt with an issue concerning the Mergers Directive 90/434 EEC, which provides for fiscal neutrality in its recitals. The Court noted that under Article 8(1) of the Directive, an exchange of shares could benefit from the tax deferral granted by the Directive.

The Court commented that by “imposing that fiscal neutrality requirement with regard to shareholders of the acquired company, Directive 90/434 aims – as stated in the first and fourth recitals in its preamble – to ensure that an exchange of shares concerning companies from different Member States is not hampered by restrictions, disadvantages or distortions arising in particular from the tax provisions of the Member States”.³²

However, the Court pointed out that “that fiscal neutrality requirement is not unconditional. Under Article 8(2) of Directive 90/434, the Member States are to make the application conditional upon the shareholders not attributing to the securities received a value for tax purposes higher than the value attributed to the securities exchanged immediately before the exchange of shares”.³³

28 *Banque Fédérative du Crédit Mutuel v Ministre de l'Économie, des Finances et de l'Industrie* (“*Banque Fédérative du Crédit Mutuel*”), C-27/07, ECLI:EU:C:2008:195.

29 *Banque Fédérative du Crédit Mutuel*, para. 24.

30 *Banque Fédérative du Crédit Mutuel*, para. 25.

31 *A.T. v Finanzamt Stuttgart-Körperschaften* (“*A.T.*”), C-285/07, ECLI:EU:C:2008:705. See - https://ec.europa.eu/taxation_customs/business/company-tax/merger-directive_en (last visited 20 Jan. 2019).

32 *A.T.*, para. 21.

33 *A.T.*, para. 22.

The Court went on to explain that “the mandatory and clear wording of Article 8(1) and (2) of Directive 90/434 offers no indication whatsoever that the Community legislature intended to leave Member States discretion with regard to implementation which would permit them to make the fiscal neutrality provided for in favour of the shareholders of the acquired company subject to additional conditions”.³⁴

The Court concluded that “to make the fiscal neutrality provided for in Article 8(1) and (2) of Directive 90/434, in relation to the exchange of shares involving companies from different Member States, subject to the additional condition that the acquiring company carry over the historical book value of the shares transferred in its tax balance sheet would be contrary to the purpose of the directive, which is to eliminate fiscal barriers to cross-border restructuring of undertakings, by ensuring that any increases in the value of shares are not taxed until their actual disposal”.³⁵

A clear outcome of this jurisprudence is that fiscal neutrality in the field of mergers, transfers, divisions and exchanges of shares is not guaranteed. It can be made subject to certain conditions by the Member States. From this it can be inferred that there is no general principle of fiscal neutrality contained in the EU Treaties. If one existed, it would be generally available in cross-border situations and there would be no need to rely on the fiscal neutrality requirement in the directive, and even that is conditional in certain situations.

The same reasoning applies in relation to the Parent Subsidiary Directive discussed above. Failure to meet the conditions contained in that Directive means that the fiscal neutrality granted under the Directive can be denied.

Article 110 TFEU

Article 110 TFEU³⁶ is found in Title VII of the TFEU under the general heading “Common Rules on Competition, Taxation and Approximation of Laws”.³⁷ It is contained in Chapter 2 under the heading “Tax Provisions”, and provides that no Member State “shall impose, directly or indirectly, on the products of other Member States any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products ... Furthermore, no Member State shall impose on the products of other Member States any internal taxation of such a nature as to afford indirect protection to other products”.

34 A.T., para. 26.

35 A.T., para. 28.

36 Formerly Article 90 EC Treaty.

37 For a copy of the Consolidated Version of the TFEU and TEU see - <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12012E/TXT&from=EN> (last visited 20 Jan. 2019)

This is the internal taxation rule which complements the provisions concerning the free movement of goods contained in Articles 28-37 TFEU. Under these provisions, customs duties on imports and exports and charges having equivalent effect are prohibited between the Member States. Article 110 TFEU complements these provisions by preventing the Member States from using their domestic tax laws to impose restrictions or tax burdens on goods from the Member States.

The Court highlighted in *Statens Control*³⁸ that “the aim of the Treaty in this field is to guarantee generally the neutrality of systems of internal taxation regarding intra-Community trade”.³⁹

In *Commission v Denmark*, the Court stressed that Article 110 TFEU⁴⁰ “must guarantee the complete neutrality of internal taxation between domestic products and imported products”.⁴¹

The purpose of Article 110 TFEU, therefore, is to ensure “that Member States do not discriminate against products originating in other Member States by favouring domestic products under their national tax legislation, thereby creating barriers to the free movement of goods between the Member States”.⁴²

Therefore, Article 110 TFEU provides a basis for application of the principle of fiscal neutrality in relation to the free movement of goods in situations covered by Article 110 TFEU only.

The Court has made it clear that since the aim of Article 110 TFEU (and its previous designations) is to ensure the free movement of goods between the Member States “in normal conditions of competition by the elimination of all forms of protection which may result from the application of internal taxation that discriminates against products from other Member States, that article must guarantee complete neutrality of internal taxation as regards competition between domestic products and imported products”.⁴³

38 *Statens Kontrol med ædle Metaller v Preben Larsen; Flemming Kjerulff v Statens Kontrol med ædle Metaller* (“*Statens Control*”), Case 142/77, ECLI:EU:C:1978:144.

39 *Statens Control*, para. 22.

40 Article 95 of the EEC Treaty at the time of the case.

41 *Commission of the European Communities v Kingdom of Denmark* (“*Commission v Denmark*”), Case 171/78, ECLI:EU:C:1980:54, para. 4.

42 *John Walker & Sons Ltd v Ministeriet for Skatter og Afgifter* (“*John Walker & Sons Ltd.*”), Case 243/84, ECLI:EU:C:1986:100, para. 20.

43 *Cámara de Comercio, Industria y Navegación de Ceuta v Ayuntamiento de Ceuta* C-45/94, para. 29.

Thus, like the fiscal neutrality concept contained in the VAT regime, here, the principle of neutrality is enshrined in Article 110 TFEU in relation to the interaction between the use of internal taxation rules and the free movement of goods.

The Fundamental Freedoms

The Court has dealt with the principle of fiscal neutrality in its jurisprudence concerning the freedom to provide services and its interaction with the direct taxation rules of the Member States.

Safir

In relation to the freedom to provide services, the Court encountered the principle of neutrality in the *Safir* case,⁴⁴ which concerned Swedish life assurance taxation rules.

According to the Swedish national court which referred the matter to the CJEU for a preliminary ruling, the aim of the Swedish rules at issue was “to ensure competitive neutrality between savings in the form of capital life assurance taken out with insurance companies established in Sweden and savings in the form of like policies taken out with companies established abroad”.⁴⁵ However, even though this was the stated aim of the national legislation in question, the Swedish tax rules at issue operated entirely differently, depending on whether the insurance companies were established in Sweden or elsewhere.

The CJEU noted that in “the perspective of a single market and in order to enable its objectives to be attained, Article 59 of the Treaty⁴⁶ ... precludes the application of any national legislation which has the effect of making the provision of services between Member States than the provision of services exclusively within one Member State”.⁴⁷

The Court determined that the Swedish legislation contained “a number of elements liable to dissuade individuals from taking out capital life assurance with companies not established in Sweden and liable to dissuade insurance companies from offering their services on the Swedish market”.⁴⁸

44 *Jessica Safir v Skattemyndigheten i Dalarnas Län, formerly Skattemyndigheten i Kopparbergs Län (“Safir”)*, C-118/96, ECLI:EU:C:1998:170.

45 *Safir*, para. 8.

46 Now Article 56 TFEU.

47 *Safir*, para. 23.

48 *Safir*, para. 30.

The Court concluded that other systems less restrictive of the freedom to provide services were conceivable, “in particular a system for charging tax on the yield on life assurance capital, calculated according to a standard method and applicable in the same way to all insurance policies, whether taken out with companies established in the Member State concerned or with companies established in another Member State”.⁴⁹

In *Safir*, the Court focused on the freedom to provide services and the principle of equal treatment. It compared the different tax treatment of a Swedish national who purchased a life assurance policy from a British insurance company with another Swedish national who purchased a similar policy from a Swedish insurance company.

The Court determined that the Swedish rules at issue amounted to less favourable tax treatment in situations where the freedom to provide (receive) services was exercised. This discriminatory tax treatment was not justified by the arguments put forward by the Swedish government. Consequently, the Swedish rules at issue amounted to a restriction on the freedom to provide services.

Interestingly, the Court made no reference to the principle of fiscal neutrality. One would think that if the principle of neutrality applied to situations covered by the fundamental freedoms that the Court would have made some reference to the principle in this case given that competitive neutrality was the objective of the national legislation at issue.

Skandia

In *Skandia*,⁵⁰ the Court faced a situation concerning Swedish tax rules which failed to grant a tax deduction to a Swedish national for pension insurance contributions paid to an insurance company established in another Member State, whereas such a tax deduction would be granted if the pension insurance premiums were paid by a Swedish resident to an insurance company established in Sweden. *Skandia* argued that such rules were incompatible with the freedom to provide services.

The CJEU accepted that the rules at issue amounted to a restriction on the freedom to provide services. The Swedish government submitted that its rules were justified by competitive neutrality.

The Swedish government explained that an employer in Sweden can deduct the costs of guaranteeing retirement pensions before actual payment of the pensions to its employees in three situations: where a reserve is created in the balance sheet

49 *Safir* para. 33.

50 *Försäkringsaktiebolaget Skandia (publ) and Ola Ramstedt v Riksskatteverket* (“*Skandia*”), C-422/01, ECLI:EU:C:2003:380.

together with an insurance credit or a guarantee; in situations where the funds are transferred to a retirement foundation or in circumstances where pension insurance premiums are paid.

The Swedish government argued that “if there were no requirement that the insurance company should be established in Sweden for pension insurance premiums to be deductible, the conditions of competition between the different ways of guaranteeing undertakings on pensions would no longer be neutral. In terms of fiscal control ... foreign branches of Swedish insurance companies and foreign insurance companies would enjoy unwarranted competitive advantages compared with other forms of management of pension capital and compared with pension insurance companies in Sweden”.⁵¹

The Court rejected these arguments, pointing out that “considerations of equality of competition between different national forms of guaranteeing undertakings on occupational pensions could not be upheld at the cost of restricting the free movement of services”.⁵²

The Court also commented that in so far as the justification based on competitive neutrality relied on the need to ensure effective fiscal controls, the Mutual Assistance Directive 77/799⁵³ could be relied on by a Member State “in order to obtain from the competent authorities of another Member State all the information enabling it to ascertain the correct amount of income tax”.⁵⁴

The Court concluded that “Article 49 EC precludes an insurance policy issued by an insurance company established in another Member State which meets the conditions laid down in national law for occupational pension insurance, apart from the condition that the policy must be issued by an insurance company operating in the national territory, from being treated differently in terms of taxation, with income tax effects which, depending on the circumstances in the individual case, may be less favourable”.

In *Skandia*, once again the Court makes no reference to the principle of fiscal neutrality and decided the case on the basis of the equal treatment principle. The rules in question were liable “both to dissuade Swedish employers from taking out occupational pension insurance with institutions established in a Member State

51 *Skandia*, para. 56.

52 *Skandia*, para. 58.

53 See https://ec.europa.eu/taxation_customs/business/tax-cooperation-control/administrative-cooperation/enhanced-administrative-cooperation-field-direct-taxation_en#heading_2 (last visited 20 Jan. 2019).

54 *Skandia*, para. 42.

other than the Kingdom of Sweden and to dissuade those institutions from offering their services on the Swedish market”.⁵⁵

The Court applied a simple restriction analysis from, first, the perspective of the employer in Sweden purchasing pension insurance from companies established in other Member States and second, from the perspective of the insurance companies selling pension insurance policies in Sweden. In both scenarios, the freedom to provide services / receive services was discouraged by the Swedish rules in question. The Court rejected the justifications put forward by the Swedish government. Accordingly, the national rules at issue amounted to a restriction on the freedom to provide services.

Amurta

In *Amurta*,⁵⁶ the Court noted the submission of the United Kingdom government that the Treaty did not guarantee “the fiscal neutrality of free movement”,⁵⁷ but made no further comment regarding the principle of fiscal neutrality in its judgment.

Emerging Markets

Finally, in *Emerging Markets*,⁵⁸ the Court dealt with a German argument which stated that the “purpose of the internal market is to ensure an efficient allocation of resources within the European Union while preserving fiscal neutrality in that market”.⁵⁹

Germany submitted that it should be able to safeguard its tax revenues and therefore, “the free movement of capital should not compel the Member States to surrender tax revenue in favour of non-member countries”.⁶⁰

The Court rejected this argument, saying that “diminution of tax revenue cannot be regarded as an overriding reason in the public interest which may be relied upon in order to justify a measure which is, in principle, contrary to a fundamental freedom”.⁶¹

55 *Skandia*, para. 28.

56 *Amurta SGPS v Inspecteur van de Belastingdienst/Amsterdam* (“*Amurta*”), C-379/05, ECLI:EU:C:2007:655.

57 *Amurta*, para. 71.

58 *Emerging Markets Series of DFA Investment Trust Company v Dyrektor Izby Skarbowej w Bydgoszczy* (“*Emerging Markets*”), C-190/12, ECLI:EU:C:2014:249.

59 *Emerging Markets*, para.101.

60 *Emerging Markets*, para.101.

61 *Emerging Markets*, para.102.

The Court made no further reference to the principle of fiscal neutrality, once again suggesting, that it is not a general principle of EU law.

The conclusion that can be drawn from this analysis is that the Court does not apply the principle of fiscal neutrality across the fundamental freedoms. Instead, it is the principle of equal treatment that is applied by the Court in its direct tax jurisprudence concerning the fundamental freedoms.

The principle of fiscal neutrality comes into play in areas such as the Parent-Subsidiary Directive, the Mergers Directive and VAT Directives where it is specifically mentioned in the secondary legislation. It is not a general principle of EU law like the principle of equal treatment even though it contains some of its features.

Part II

Introduction

Schön acknowledges that “the ECJ has, in many instances, held that the compatibility of one Member State’s legislation with the Internal Market might depend on existing legislation in other Member States”. He argues that this expansion of the ‘unilateral non-discrimination test’ goes beyond “what is required by the principle of neutrality as framed by the Internal Market”.⁶²

Schön discusses specific examples in the Court’s direct tax jurisprudence, including *Bouanich II*,⁶³ where he points out that a “true one dimensional, non-discrimination test of a Member State’s legislation with regard to taxation must regard the legislations of the other Member States to be virtually non-existent”.

62 See section 2.3.4.1 on page 277. Again, this view is not in keeping with the Court’s direct tax jurisprudence concerning the principle of equal treatment. In an outbound dividend situation, if a withholding tax is imposed, whilst none is imposed domestically, a restriction on the exercise of a fundamental freedom takes place because freedom of establishment or the free movement capital may be hindered. However, if under a double tax convention (DTC) that withholding tax is fully relieved in the other Member State, then the restriction is healed and disappears. In such circumstances, the Court takes the tax treatment under the DTC into account because DTCs form part of the legal framework in the case. See *Margaretha Bouanich v Skatteverket* (“*Bouanich I*”), C-265/04, ECLI:EU:C:2006:51, para. 48 et seq. The Court accepted that the restriction on the free movement of capital could be remedied under the DTC if equal treatment was ensured. See also, *Amurta SGPS v Inspecteur van de Belastingdienst/Amsterdam* (“*Amurta*”), C-379/05, ECLI:EU:C:2007:655, para. 80. For analysis, see Tom O’Shea, “*ECJ Strikes Down Dutch Taxation of Dividends*”, Tax Notes International, Jan. 14, 2008, 103-106.

63 *Margaretha Bouanich v Directeur des services fiscaux de la Drôme* (“*Bouanich II*”), C-375/12, ECLI:EU:C:2014:138. For this author’s analysis, see Tom O’Shea, “*CJEU Finds Former French Tax Shield Incompatible with EU Law*”, Tax Notes International, Aug. 18, 2014, 2014, 545-548.

In relation to the Court's outbound dividend cases, such as *Amurta* and *Commission v Italy* ("*Outbound Dividends*"),⁶⁴ Schön argues that the CJEU's jurisprudence has "given rise to misunderstandings and uncertainty when the judges declared that a withholding tax on an outbound dividend payment, which in principle infringes on the free movement of capital, might be redeemed by the willingness of the residence Member State of the recipient to grant a tax credit for such withholding tax under a tax treaty".⁶⁵

Schön goes on to criticise the Court's *Schumacker* line of cases,⁶⁶ arguing that a "unilateral view on tax neutrality would simply require each Member State to apply its domestic rules on deductions and similar benefits in a non-discriminatory fashion to cross-border situations".⁶⁷

Moreover, Schön rebukes the Court for its cross-border loss jurisprudence, in particular, its *Marks & Spencer* judgment⁶⁸ and its subsequent line of cases, commenting that a "similar strand of judicature concerns cross-border deductibility of losses, where the ECJ has held that the residence Member State might be required to extend its beneficial rules on loss compensation for domestic subsidiaries and permanent establishments (PEs) to foreign subsidiaries and PEs to ensure a one-off deduction for the taxpayer if the taxpayer cannot deduct these losses in the source Member State".⁶⁹

Schön concludes that the "ECJ, in particular, grants the Member States limited discretion to take unilateral action against the possible "double deduction" of losses in both of the Member States involved".⁷⁰

64 *Commission v Italy* ("*Outbound Dividends*"), C-540/07, ECLI:EU:C:2009:717, para. 37. The Court explained that it was necessary for that purpose "that application of the double taxation convention allow the effects of the difference in treatment under national legislation to be compensated for. The difference in treatment between dividends distributed to companies established in other Member States and those distributed to resident companies does not totally disappear unless the tax withheld at source under national legislation can be set off against the tax due in the other Member State in the full amount of the difference in treatment arising under the national legislation."

65 Section 2.3.4.2 on p 277.

66 *Finanzamt Köln-Alstadt v Roland Schumacker* ("*Schumacker*"), C-279/93, ECLI:EU:C:1995:31.

67 Section 2.3.4.3 on p 278.

68 *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes)* ("*Marks & Spencer*"), C-446/03, ECLI:EU:C:2005:763.

69 Section 2.3.4.3 on p 278.

70 Section 2.3.4.3 on p 278. The Court disagreed with Schön in *Marks & Spencer*. In that judgment, the Court allowed a Member State to prevent "double deduction" of losses, since cross-border loss relief did not have to be granted in situations where the "no possibilities test" (contained in paragraph 55 of the judgment) was not met. It did the same in subsequent cases.

In Part II, an attempt will be made to respond to some of Professor Schön's criticisms of the Court's jurisprudence.

Inconsistencies

These inconsistencies with the principle of international fiscal neutrality in the Court's direct tax jurisprudence are brought to our attention by Schön, but at no time does he question whether the principle of fiscal neutrality actually applies across the Court's jurisprudence on the fundamental freedoms, like the principle of equal treatment. Instead, on the assumption that the principle of fiscal neutrality is a "concept of EU law", he highlights a number of situations where the Court's case law is not in keeping with that principle without ever questioning why that is the situation.

Equal Treatment Principle

Taking the *Bouanich II*, *Schumacker*, *Amurta*, *Mark & Spencer* cases discussed by Schön, as a starting point, one can immediately see that there is an alternative legal principle operating in the Court's case law, that is based on the principle of equal treatment and not on the principle of fiscal neutrality.

The principle of equal treatment is often referred to by the Court as the "principle of national treatment", or by this author, sometimes, as a "migrant/non-migrant test".⁷¹ However, as has been shown in Part I, this principle is not the same as the principle of fiscal neutrality.

Schön argues that "the fundamental freedoms prohibit any domestic legislation that separates domestic economic activities and cross-border economic activities". In support of his argument he cites *Avoir Fiscal*⁷² para. 24; *Schumacker* paras. 20-24; *Asscher*⁷³ para. 36 and *Commission v Portugal* ("*CGT Exemption*"),⁷⁴ para. 15. However, an examination of these cases demonstrates that the Court simply applied the national treatment principle in each case.

See, more recently, *NN A/S v Skatteministeriet* ("*NN*"), C-28/17, ECLI:EU:C:2018:526, para. 42 et seq. where the Court applied its *Marks & Spencer*'s reasoning.

71 See Chapter 1 and Conclusions of Tom O'Shea, *EU Tax Law and Double Tax Conventions*, supra, and this author's comments from the 2006 transcript of the first *Avoir Fiscal* EU Tax Conference, London: "*From Avoir Fiscal to Marks & Spencer*", Tax Notes International, May. 15, 2006, 587-612 at 604.

72 *Commission v France* ("*Avoir Fiscal*") Case 270/83, ECLI:EU:C:1986:37.

73 *P. H. Asscher v Staatssecretaris van Financiën* ("*Asscher*"), C-107/94, ECLI:EU:C:1996:251.

74 *Commission v Portugal* ("*CGT Exemption*"), C-345/05, ECLI:EU:C:2006:685.

Avoir Fiscal

In *Avoir Fiscal* para. 24, the Court explained that “Article 52 of the EEC Treaty prohibits the Member States from laying down in their laws conditions for the pursuit of activities by persons exercising their right of establishment which differ from those laid down for its own nationals”.

This is the national (equal) treatment principle. It is clearly set out in the freedom of establishment’ provisions of the TFEU.

Schumacker

In *Schumacker* para. 24, the Court concluded that the free movement of workers “does not allow a Member State, as regards the collection of direct taxes, to treat a national of another Member State employed in the territory of the first Member State in the exercise of his right of freedom of movement less favourably than one of its own nationals in the same situation”. This is another clear statement of the national treatment principle by the Court.

Biehl

In *Schumacker* paragraph 23, the Court cited its earlier *Biehl* case,⁷⁵ where it had specifically referred to the principle of equal treatment, pointing out that “the principle of equal treatment with regard to remuneration would be rendered ineffective if it could be undermined by discriminatory national provisions on income tax. That is why the Council laid down the requirement in Article 7 of Regulation ... 1612/68 ... on the free movement of workers ... that workers who are nationals of a Member State are to enjoy, in the territory of another Member State, the same tax benefits as nationals there”.

These statements from *Schumacker* and *Biehl* provide further support for the argument that it is the principle of national treatment that is being applied by the Court.

Comparator

In *Papillon*,⁷⁶ the Court pointed out that in order to determine “whether discrimination exists, the comparability of a Community situation with one which is purely domestic

75 *Klaus Biehl v Administration des contributions du grand-duché de Luxembourg* (“*Biehl*”), C-175/88, ECLI:EU:C:1990:186.

76 *Société Papillon v Ministère du Budget, des Comptes publics et de la Fonction publique* (“*Papillon*”), C-418/07, ECLI:EU:C:2008:659. The Court confirmed this same reasoning in the later cases of *Accor*, para. 62; *Commission v Hungary* (“*Principal Private Residence*”), para. 61 and in *SCA*, para. 27, where the Court removed the reference to “Community situations” and instead, inserted “cross-border situations”. See *Ministre du Budget, des Comptes publics et de la Fonction publique v Accor SA* (“*Accor*”), C-310/09,

must be examined by taking into account the objective pursued by the national provisions at issue". Thus, in determining whether a situation constitutes discrimination or a restriction on the exercise of a fundamental freedom, the comparator to be used in most ⁷⁷ scenarios is the cross-border situation compared to a similar domestic situation. This applies to both origin and host Member State situations.

The Court made this clear in paragraph 94 of *De Groot*,⁷⁸ where the Court directed that "as far as the exercise of the power of taxation so allocated is concerned, the Member States must comply with the Community rules ... and, more particularly, respect the principle of national treatment of nationals of other Member States and of their own nationals who exercise the freedoms guaranteed by the Treaty".⁷⁹ However, this test is not the same as the fiscal neutrality test suggested by Schön because all foreign situations do not have to be treated in the same way as domestic situations.

A foreign situation only has to be treated in a similar way to a domestic situation where (a) one of the fundamental freedoms or EU citizenship rights is being exercised and (b) the foreign situation is comparable to a domestic situation and there is no general interest justification available to justify the difference in treatment of the cross-border situation. This is the principle of national treatment or equal treatment expressed above in paragraph 94 of *De Groot* and in paragraph 24 of *Sauvage*. This equal treatment principle is applied by the Court across the fundamental freedoms and in relation to EU citizenship rights.

Support for this argument is found in the Court's tax and non-tax jurisprudence involving the exercise of the fundamental freedoms.

ECLI:EU:C:2011:581; *Commission v Hungary* ("Principal Private Residence"), C-253/09, ECLI:EU:C:2011:795; and *Inspecteur van de Belastingdienst/Noord/kantoor Groningen and Others v SCA Group Holding BV and Others* ("SCA"), C-39/13, ECLI:EU:C:2014:1758.

77 At present, there is one example in the Court's direct tax case law where the comparator involved the different tax treatment two cross-border workers exercising free movement of workers in the host Member State: *C.G. Sopora v Staatssecretaris van Financiën* ("*Sopora*") C-512/13, ECLI:EU:C:2015:108. For an in-depth analysis of the *Sopora* case, see Tom O'Shea, "Dutch Treatment of Two Nonresident Workers May Be Contrary to EU Law", *Tax Notes International*, Aug. 31, 2015, 863-866.

78 *F.W.L. de Groot v Staatssecretaris van Financiën* ("*De Groot*"), C-385/00, ECLI:EU:C:2002:750.

79 In *Sauvage*, para. 24, the Court made it clear that it was speaking about the equal treatment principle: "... the Member States must comply with EU rules and, more particularly, observe the principle of equal treatment". *Benoît Sauvage and Kristel Lejeune v État belge* ("*Sauvage*"), C-602/17, ECLI:EU:C:2018:856.

Free Movement of Workers

Sagulo

In *Sagulo*,⁸⁰ for example, the Court dealt with a free movement of workers' case involving the non-production of a valid identity card. As a result, the foreign worker was subjected to a heavy penalty, but a much lighter one was imposed on a host State national for a similar offence.

The Court pointed out that foreign workers could be subject to different penal provisions compared with host State nationals who infringe an obligation concerning identity documents. However, the Court stressed that in "the absence of a criterion which in the present case might be based on the principle of national treatment contained in Article 7 of the Treaty, it is nevertheless to be observed that although Member States are entitled to impose reasonable penalties for infringement by persons subject to Community law of the obligation to obtain a valid identity card or passport, such penalties should by no means be so severe as to cause an obstacle to the freedom of entry and residence provided for in the Treaty. To this extent it cannot be ruled out that the penalties ... are not compatible with the requirements of Community law which is based on the freedom of movement of persons and, apart from certain exceptions, on the general application of the principle of equal treatment with nationals. If the Member State has not adapted its legal provisions to the requirements of Community law in this sphere, it is the task for the national court to use its judicial discretion to impose a punishment appropriate to the character and objective of the provisions of Community law, the observance of which the penalty is intended to safeguard".⁸¹

In *Sagulo*, the Court clearly applied the principle of equal treatment, linking it with the different treatment of a foreign national in the host Member State compared to a host State national. The Court also explained that the national treatment principle is contained in the non-discrimination principle which is set out in Article 7 of the EEC Treaty (now Article 18 TFEU).

Emir Gül

In another free movement of workers' case, *Emir Gül*,⁸² which concerned Article 3(1) of Regulation 1612/86,⁸³ the Court, referring to the preamble of that Regulation, noted

80 *Concetta Sagulo, Gennaro Brenca and Addelmadjid Bakhouché* ("*Sagulo*"), Case 8/77, ECLI:EU:C:1977:131.

81 *Sagulo*, para. 12.

82 *Emir Gül v Regierungspräsident Düsseldorf* ("*Emir Gül*"), Case 131/85, ECLI:EU:C:1986:200.

83 Regulation 1612/68 expanded the free movement of workers to include the right to obtain the "same tax and social advantages", in the host Member State, as host State nationals. See

that “equal treatment must be ensured ‘in fact and in law’ between foreign workers exercising free movement of workers’ rights and host State workers.”⁸⁴

The Court pointed out that Articles 10 and 11 of Regulation 1612/68 granted rights to the spouses of workers and that these rights were linked to the rights which the worker enjoys under Article 48 of the EEC Treaty (now Article 45 TFEU). It emphasised that in so far as “the spouse can rely on such secondary rights and those rights include the right to take up any activity as an employed person pursuant to Article 11, he must be able to pursue that activity under the same conditions as are applicable to a worker entitled to freedom of movement. Article 3 (1) of the regulation thus requires the authorities of the host Member State to treat the spouse in a non-discriminatory fashion. The ‘national treatment’ to which workers from Member States are entitled in that regard is thus extended to their spouses.”⁸⁵

In that context, the Court observed that “the first indent of Article 3(1) of the Regulation prohibits the application of discriminatory legal provisions and ‘administrative practices’ which make access to employment subject to conditions not applicable to nationals of the host State. Furthermore, the very concept of equal treatment presupposes not only that the same laws should be applied to nationals and to foreigners but that those laws should be applied to both categories of person in the same manner.”⁸⁶

Daily Mail

In *Daily Mail*,⁸⁷ the Court highlighted, that even though the freedom of establishment provisions are directed mainly to ensuring that foreign nationals and companies are treated in the host Member State in the same way as nationals of that State, they also prohibit the Member State of origin from hindering the establishment in another Member State of one of its nationals.”⁸⁸

De Groot

In the landmark direct tax case, *De Groot*, the Court explained that national rules which “preclude or deter a national of a Member State from leaving his country of origin to exercise his right of free movement therefore constitute an obstacle to that

Article 7(2) – <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:31968R1612&from=EN> (last accessed 20 Jan. 2019).

84 Regulation 1612/68 Preamble (fifth recital).

85 *Emir Gül*, para. 20.

86 *Emir Gül*, para. 25.

87 *The Queen v H. M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust plc* (“*Daily Mail*”), Case 81/87, ECLI:EU:C:1988:456.

88 *Daily Mail*, para. 16.

freedom even if they apply without regard to the nationality of the workers concerned”.⁸⁹

This statement shows that the national treatment principle operates from both an origin Member State and a host Member State perspective.

De Groot is an early example of an origin Member State case, where the national treatment principle was applied by the Court from an origin Member State perspective. It may be contrasted with *Schumacker*, where the national treatment principle was applied from a host Member State perspective.

In *De Groot*, the Court applied its *Daily Mail*⁹⁰ reasoning and confirmed that from an origin Member State perspective, the national tax rule causing the problem may be prohibited even though it does not discriminate on grounds of nationality.

This is important because the comparator from an origin Member State perspective usually involves two origin Member State nationals, one of whom is exercising a fundamental freedom, like Mr De Groot, while the other is operating in that origin Member State. Sometimes the national tax rule may discriminate based on the place of investment or based on the place where an establishment is created but, generally speaking, from an origin Member State standpoint, the national tax rule will be analysed from a restriction on the exercise of a fundamental freedom angle.

The Court’s clear explanation of the scope of the national treatment principle in paragraph 94 of *De Groot* is extremely important for understanding what the Court is saying in its fundamental freedom cases. The reference to “nationals of other Member States” generally refers to host State situations, whereas the reference to “own nationals” refers to origin Member State scenarios.⁹¹ The national treatment principle applies from both perspectives.

One further paragraph in the *De Groot* judgment should be considered for the purposes of the present discussion. In paragraph 114, the Court highlighted that “Community law lays down no specific requirement with regard to the way in which the State of residence must take account of the personal and family circumstances of a worker who, during a particular tax year, received income in that State and in another

89 *De Groot*, para. 78.

90 *Daily Mail*, para. 16.

91 This is not always the case. There are examples in the Court’s jurisprudence where a host Member State national left his origin Member State to “switch-on” EU law rights by becoming a worker in another Member State. When that person returned to his origin Member State, he now entered his origin Member State as an EU worker with the right to work and to establish himself in his origin Member State, together with all the related EU law rights. A good example is seen in *The Queen v Immigration Appeal Tribunal and Surinder Singh, ex parte Secretary of State for Home Department* (“*Surinder Singh*”), C-370/90, ECLI:EU:C:1992:296, paras. 19-21.

Member State. However, ... the conditions governing the way in which the State of residence takes into account such a taxpayer's personal and family circumstances must not constitute discrimination, either direct or indirect, on grounds of nationality, or an obstacle to the exercise of a fundamental freedom guaranteed by the Treaty".⁹²

This is an important clarification regarding the scope of the national treatment principle because the Court makes it clear that a taxpayer can suffer discrimination on grounds of nationality, direct or indirect discrimination, and may also be impeded in the exercise of a fundamental freedom by a rule which amounts to a restriction or an obstacle to the exercise of a freedom.⁹³

As the author has pointed out already,⁹⁴ from an origin Member State perspective, the comparator will usually involve two origin Member State nationals, one of whom is exercising a fundamental freedom. Consequently, generally speaking, the national rule at issue will constitute a restriction on the exercise of the freedom, since an origin Member State does not usually discriminate on grounds of nationality, directly or indirectly, against its own nationals.

This means that discrimination on grounds of nationality, directly or indirectly, will apply only in host State situations since the comparator in a host State scenario will usually involve a foreigner.

In *De Groot* paragraph 114, the Court confirms this thinking. Since discrimination on grounds of nationality, both direct and indirect, only occurs from a host Member State

92 *De Groot*, para. 114.

93 An obstacle to the exercise of a fundamental freedom may be caused by two types of non-discriminatory tax rule. First, by a tax rule which treats the cross-border situation less favourably than a comparable domestic situation, as seen in *De Groot*, *Marks & Spencer* and *Cadbury Schweppes*. See *Cadbury Schweppes plc and Cadbury Schweppes Overseas Ltd v Commissioners of Inland Revenue* ("*Cadbury Schweppes*"), C-196/04, ECLI:EU:C:2006:544. Second, an obstacle to the exercise of a fundamental freedom may exist where the cross-border and domestic situation are treated in the same way (an "even-handed tax rule") but the national rule still constitutes a restriction on the exercise of the freedom. Examples are seen in cases like *Bosman* and *Biehl*. See *Union royale belge des sociétés de football association ASBL v Jean-Marc Bosman, Royal club liégeois SA v Jean-Marc Bosman and others* and *Union des associations européennes de football (UEFA) v Jean-Marc Bosman* ("*Bosman*"), C-415/93, ECLI:EU:C:1995:463 and *Klaus Biehl v Administration des contributions du grand-duché de Luxembourg* ("*Biehl*"), C-175/88, ECLI:EU:C:1990:186. Examples concerning freedom of establishment, are seen in cases like *Futura* and *CaixaBank*. See *Futura Participations SA and Singer v Administration des contributions* ("*Futura*"), C-250/95 and *CaixaBank France v Ministère de l'Économie, des Finances et de l'Industrie* ("*CaixaBank*"), C-442/02, ECLI:EU:C:2004:586.

94 See Tom O'Shea, "European Tax Controversies: A British-Dutch Debate: Back to Basics and Is the ECJ Consistent?" (2013) WTJ, 1, 100-127.

point of view, the approach taken by the Court in its analysis in “host State” judgments may differ considerably from those involving “origin State” scenarios.⁹⁵

In origin Member State cases, the judgment of the Court will focus on a restriction analysis.⁹⁶ In host Member State situations, a discrimination or restriction approach may be adopted (sometimes, both), since most host State cases will involve the different treatment of an EU national from another Member State and it is possible to directly discriminate on grounds of nationality (*Avoir Fiscal*), indirectly discriminate (*Biehl*) or merely restrict (*Futura*)⁹⁷ the exercise of a fundamental freedom. Both discrimination and restriction approaches may need to be adopted in situations where the Court finds no discrimination on grounds of nationality. In such cases, the Court may still need to investigate whether or not a restriction on the exercise of a fundamental freedom exists. Two examples where this occurred in the Court’s direct tax jurisprudence are *Futura* and *Truck Center*.⁹⁸

This means that the host and origin constellations should be analysed separately, even though the same principle of equal treatment is applied from either the perspective of a host Member State environment or from the standpoint of an origin Member State. This explanation as to how the national treatment principle works from the host/origin perspectives is clearly visible from paragraph 94 of the *De Groot* judgment.

95 This insight helps to explain much of the criticism of the Court in the scholarly literature. See Tom O’Shea, “*European Tax Controversies: Quis Custodiet Ipsos Custodes?*” ECTJ, 2011-12, 1, 39-98.

96 See, for example, *Marks & Spencer*, where the concept of discrimination does not get a mention in the Court’s judgment, despite the focus on the concept of discrimination at the national level (Special Commissioners’ judgment) and in the Opinion of Advocate General Poiares Maduro. If discrimination is considered from an origin State perspective, it will usually involve discrimination based on the place of establishment or on the place of investment. Neither of these involve discrimination on grounds of nationality and will be treated in the same way as a restriction on the exercise of a fundamental freedom.

97 See *Futura Participations SA and Singer v Administration des contributions* (“*Futura*”), C-250/95, ECLI:EU:C:1997:239.

98 *Belgian State - SPF Finances v Truck Center SA* (“*Truck Center*”), C-282/07, ECLI:EU:C:2008:762. For a detailed analysis by this author, see Tom O’Shea, “*Truck Center: A Lesson in Source Vs. Residence Obligations in the EU*”, Tax Notes International, Feb. 16, 2009, 593-601. In *Futura*, the Court conducted a discrimination analysis and determined there was no discrimination. It then carried out a restriction analysis and concluded that the Luxembourg rules constituted a restriction on the freedom of establishment that was not justified when the principle of proportionality was taken into consideration. In *Truck Center*, the Court determined that there was no discrimination, since the cross-border situation was not comparable to the domestic. Next, it performed a restriction analysis and determined that there was neither a restriction on the freedom of establishment nor on the free movement of capital.

Freedom of Establishment

In the field of freedom of establishment, the Court has also confirmed the application of the national treatment principle from both a host Member State and origin Member State perspective.

Host State

Commission v Italy ("Housing Aid")

In *Commission v Italy ("Housing Aid")*,⁹⁹ the Court highlighted that "Articles 52 and 59 of the Treaty are essentially intended to give effect, in the field of activities as self-employed persons, to the principle of equal treatment enshrined in Article 7 of the Treaty..."¹⁰⁰

The Court explained that these two Articles of the Treaty are intended "to secure the benefit of national treatment for a national of a Member State who wishes to pursue an activity as a self-employed person in another Member State and they prohibit all discrimination on grounds of nationality resulting from national or regional legislation and preventing the taking up or the pursuit of such an activity".¹⁰¹

The Court stressed that foreigners who go to the host Member State to conduct an economic activity must have access to housing, including social housing, on conditions equivalent to host State nationals. It indicated that housing legislation was "subject to the principle of national treatment".¹⁰² It went on to conclude that service-providers might also require housing in the host Member State on a permanent basis. The Court determined that "no distinction can be drawn between different forms of establishment and that providers of services cannot be excluded from the benefit of the fundamental principle of national treatment".¹⁰³ Accordingly, the Italian housing legislation which restricted certain advantages to Italian nationals was incompatible with Italy's obligations under Articles 52 and 59 of the EEC Treaty (now Article 49 and 56 TFEU).

Avoir Fiscal

In *Commission v France ("Avoir Fiscal")*,¹⁰⁴ the European Commission brought infringement proceedings against France, complaining that foreign companies

99 *Commission v Italy ("Housing Aid")*, Case 63/86, ECLI:EU:C:1988:9.

100 *Commission v Italy ("Housing Aid")*, para. 12.

101 *Commission v Italy ("Housing Aid")*, para. 13.

102 *Commission v Italy ("Housing Aid")*, para. 17.

103 *Commission v Italy ("Housing Aid")*, para. 19.

104 *Commission v France ("Avoir Fiscal")*, Case 270/83, ECLI:EU:C:1986:37.

operating in France via a branch were not given the same tax treatment as a French company. In other words, they were denied national treatment in France even though they were in a comparable situation to a French company from the point of view of the French corporate tax system.

Under the French legislation, the benefit of the shareholders' tax credit (otherwise, 'avoir fiscal') was reserved for companies with their habitual residence or registered office in France. Companies from other States with branches in France did not meet this criterion.

The Court stated that - "Article 52 of the EEC Treaty embodies one of the fundamental principles of the Community and has been directly applicable in the Member States since the end of the transitional period. By virtue of that provision, freedom of establishment for nationals of one Member State on the territory of another includes the right to take up and pursue activities as self-employed persons and to set up and manage undertakings under the conditions laid down for its own nationals by the law of the country where such establishment is effected. The abolition of restrictions on freedom of establishment also applies to restrictions on the setting up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State".¹⁰⁵

The Court observed in paragraph 16 that "insurance companies whose registered office is in another Member State and who pursue their activities in France through branches or agencies are thus not treated in the same way as insurance companies whose registered office is in France. It noted that "French tax law does not distinguish, for the purpose of determining the income liable to corporation tax, between companies having their registered office in France and branches and agencies situated in France of companies whose registered office is abroad".¹⁰⁶ In other words, the comparator in the host State environment involves the different treatment of the non-resident company with the French branch with a French resident company.

The Court explained, in paragraph 20: "Since the rules at issue place companies whose registered office is in France and branches and agencies situated in France of companies whose registered office is abroad on the same footing for the purposes of taxing their profits, those rules, cannot, without giving rise to discrimination, treat them differently in regard to the grant of an advantage related to taxation, such as shareholders' tax credits.

By treating the two forms of establishment in the same way for the purposes of taxing their profits, the French legislature has in fact admitted that there is no objective difference between their positions in regard to the detailed rules and conditions relating to that taxation which could justify different treatment".

105 *Avoir Fiscal*, para. 13.

106 *Avoir Fiscal*, para. 19.

The Court concluded with a clear statement of the national treatment principle, which it noted was set out in the freedom of establishment provisions of the Treaty of Rome: “Article 52 of the EEC Treaty prohibits the Member States from laying down in their laws conditions for the pursuit of activities by persons exercising their right of establishment which differ from those laid down for its own nationals”.¹⁰⁷

Origin State

Marks & Spencer

In relation to origin State situations concerning the freedom of establishment, the *Marks & Spencer* judgment¹⁰⁸ is a leading example.

In *Marks & Spencer*, the United Kingdom parent company established subsidiaries in other Member States. These subsidiaries made losses and after a number of years, the parent company decided to close down these cross-border operations and claim United Kingdom group relief for the foreign losses. The United Kingdom authorities refused to grant this cross-border loss relief since the subsidiaries were established in other Member States and not in the United Kingdom. The parent company argued that this tax treatment was in breach of the freedom of establishment.

The Court determined that the exclusion of the group relief tax advantage “in respect of the losses incurred by a subsidiary established in another Member State which does not conduct any trading activities in the parent company’s Member State is of such a kind as to hinder the exercise by that parent company of its freedom of establishment by deterring it from setting up subsidiaries in other Member States”.¹⁰⁹

In other words, the United Kingdom’s group relief rules amounted to a restriction on the exercise of the freedom of establishment by the United Kingdom parent company since “it applies different treatment for tax purposes to losses incurred by a resident subsidiary and losses incurred by a non-resident subsidiary”.¹¹⁰

The *Marks & Spencer* judgment is an example of an origin State rule that treated two United Kingdom parent companies differently: a United Kingdom company with a foreign subsidiary was treated less favourably than a United Kingdom company with a United Kingdom subsidiary.

107 *Avoir Fiscal*, para. 24.

108 *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes)* (“*Marks & Spencer*”), C-446/03, ECLI:EU:C:2005:763.

109 *Marks & Spencer*, para. 33.

110 *Marks & Spencer*, para. 13.

This is an application of the equal treatment / national treatment principle from an origin State perspective. Further examples are seen in the Court's jurisprudence, including *Keller Holding*.¹¹¹

Keller Holding

Subsequent to the *Marks & Spencer* judgment, in *Keller Holding*, the Court dealt with a case involving a German parent company which owned an Austrian indirect subsidiary via a German subsidiary. The German parent company was denied a deduction for its financing costs related to the Austrian company because the dividends paid by that Austrian company to its German parent company were exempt from tax in Germany under the Austro-German Double Tax Convention. However, a German parent company that indirectly owned a German sub-subsidiary via a German subsidiary was allowed to deduct the financing costs linked to its German sub-subsidiary. *Keller Holding* submitted that these German rules were in breach of the freedom of establishment.

The Court agreed, highlighting that because of that difference in treatment, “a parent company might be dissuaded from carrying on its activities through the intermediary of subsidiaries or indirect subsidiaries established in other Member States”.

In other words, the Court applied the national treatment principle from an origin Member State perspective: the tax position of a German parent company having an indirect subsidiary in another Member State was less favourable than if it has established its sub-subsidiary in Germany. This difference in tax treatment between two German parent companies constituted a restriction on the freedom of establishment.

The Court explained that the “difference in tax treatment at issue ... relates to parent companies according to whether or not they have indirect subsidiaries in Germany, even though those parent companies are all established in that Member State. As far as the tax situation of the latter is concerned as regards the dividends paid by their indirect subsidiaries, the fact remains that those dividends do not give rise to tax being levied on the parent companies, whether they are derived from indirect subsidiaries taxable in Germany or in Austria”.¹¹²

In terms of comparability between the two parent companies, the Court noted that “as far as the taxation of dividends received is concerned, parent companies subject to unlimited tax liability in Germany are in a comparable position whether they receive dividends from an indirect subsidiary established in that Member State or from an indirect subsidiary having its registered office in Austria.

111 *Finanzamt Offenbach am Main-Land v Keller Holding GmbH* (“*Keller Holding*”), C-471/04, ECLI:EU:C:2006:143.

112 *Keller Holding*, para. 38.

In both cases, the dividends received by the parent company were, in reality, exempt from tax. Accordingly, the Court held that a restriction on the deductibility of a parent company's financing costs – as a corollary of the non-taxation of dividends – which affects solely dividends from abroad does not reflect a difference in the situation of parent companies according to whether the indirect subsidiary owned by the latter has its registered office in Germany or in another Member State.¹¹³

Freedom to Provide (Receive) Services

The national treatment principle has also been applied in relation to the freedom to provide services. Two classic examples in the direct tax area are *Vestergaard*¹¹⁴ (origin Member State) and *Gerritse*¹¹⁵ (host Member State).

Origin State

Safir

In *Safir*, discussed above, the Court indicated that the Swedish legislation contained a number of elements liable to dissuade people from taking out life assurance with companies established outside Sweden and also, that that legislation was liable to dissuade insurance companies from offering their services on the Swedish market.

The Court applied the national treatment principle from an origin Member State perspective, highlighting that “Article 59 of the Treaty likewise precludes the application of any national legislation which has the effect of making the provision of services between Member States more difficult than the provision of services within one Member State”.¹¹⁶

Safir was domiciled in Sweden and was affected by a Swedish tax rule when she took out a life assurance policy with a British insurance company, Skandia Life, that was operating in the Swedish market. The Swedish legislation established a different tax regime for capital life assurance policies, depending on whether they were taken out with companies established in Sweden or with companies established elsewhere.

Vestergaard

In *Vestergaard*, another origin State case, the Court examined Danish rules which denied a tax deduction for expenses related to the attendance at a training course held

113 *Keller Holding*, para. 37.

114 *Skatteministeriet v Bent Vestergaard* (“*Vestergaard*”), C-55/98, ECLI:EU:C:1999:533.

115 *Arnoud Gerritse v Finanzamt Neukölln-Nord* (“*Gerritse*”), C-234/01, ECLI:EU:C:2003:340.

116 *Jessica Safir v Skattemyndigheten i Dalarnas Län, formerly Skattemyndigheten i Kopparbergs Län* (“*Safir*”), C-118/96, ECLI:EU:C:1998:170, para. 23.

outside Denmark, even though a tax deduction was granted for similar training courses held in Denmark.

The Danish rules denied the deduction because it was assumed that there was a significant tourism element involved, however, the same assumption was not made in relation to similar training courses held at tourist resorts in Denmark.

The Court noted that such rules involved “a difference in treatment based on the place where the service is provided prohibited by Article 59 of the Treaty”.¹¹⁷

Host State

Tax rules in host Member States have also been challenged before the Court in relation to freedom to provide services.

Hubbard

In *Hubbard*,¹¹⁸ a case concerning a cross-border provision of services by an executor, the Court applied the national treatment principle in relation to national legislation in the host Member State which required a foreign executor to provide security for costs because he brought an action before the courts of the host Member State, whilst host State nationals were not subject to such a requirement. The Court decided that such legislation constituted discrimination on grounds of nationality.¹¹⁹

De Coster

In *De Coster*,¹²⁰ Belgian rules which imposed a tax on satellite dishes, whilst the transmission of programmes by national cable operators was uncharged.

The Court pointed out that such rules were “liable to impede more the activities of operators ... established in Member States other than the Kingdom of Belgium, while giving an advantage to the internal Belgian market and to radio and television within that Member State”.¹²¹

The Court applied the national treatment from a host Member State perspective. The service provider established in a Member State outside Belgium was entitled to no

117 *Vestergaard*, para. 22.

118 *Anthony Hubbard (Testamentvollstrecker) v Peter Hamburger (“Hubbard”)* C-20/92, ECLI:EU:C:1993:280.

119 *Hubbard*, para.14.

120 *François De Coster v Collège des bourgmestre et échevins de Watermael-Boitsfort (“De Coster”)*, C-17/00, ECLI:EU:C:2001:651.

121 *De Coster*, para. 35.

less favourable tax treatment in the host Member State (Belgium) than that given to Belgian service providers.

Gerritse

Similarly, in *Gerritse*,¹²² the Court faced German rules which taxed a foreign service-provider in Germany on a gross income basis with no deduction for his business expenses taken into consideration, whereas a similar German service-provider was taxed on a net income basis after taking account of his business expenses.

The Court determined that such rules risk “operating mainly to the detriment of nationals of other Member States and therefore constitutes indirect discrimination on grounds of nationality, contrary in principle to Articles 59 and 60 of the Treaty”.¹²³

The Court explained that the business expenses in question are “directly linked to the activity that generated the taxable income in Germany, so that residents and non-residents are in a comparable situation in that respect”.¹²⁴

Free Movement of Capital

In relation to the free movement of capital, the Court has also applied the national treatment principle from both an origin Member State and a host Member State perspective.

Origin State

Manninen

Schön’s analysis of *Manninen*¹²⁵ is flawed because it fails to take into account how the principle of equal treatment operates, in a free movement of capital situation, from an origin Member State perspective.

In *Manninen*, the Finnish rules at issue eliminated the problem of economic double taxation domestically through the provision of a tax credit linked to the corporation tax paid by the Finnish dividend distributing company. The aim of the Finnish legislation was to ensure that Finnish residents received a tax credit that left them tax free on that dividend income.

122 *Arnoud Gerritse v Finanzamt Neukölln-Nord* (“*Gerritse*”), C-234/01, ECLI:EU:C:2003:340.

123 *Gerritse*, para 28.

124 *Gerritse*, para 27.

125 *Petri Manninen* (“*Manninen*”), C-319/02, ECLI:EU:C:2004:484.

When a Finnish resident like Manninen invested abroad, in a Swedish company, and received a dividend, Finland granted no tax credit. Instead, it taxed that income in the hands of its Finnish resident. The Court held that this less favourable tax treatment constituted a restriction on the free movement of capital in situations where the Swedish company paid corporation tax in Sweden. In coming to this conclusion, the Court applied the national treatment test from an origin Member State perspective.

Since Manninen suffered economic double taxation when he invested in the Swedish company, he was entitled to similar relief in Finland to that granted to a Finnish investor in a Finnish company.

No fiscal neutrality was guaranteed in this case, however, because, if the rate of taxation in Sweden was higher than Finland, Finland was not obliged to grant a tax credit at a rate higher than the Finnish rate, since to do so would undermine the Finnish tax regime and go beyond what was required by the equal treatment principle.¹²⁶

The Court also made it clear that Finland did not have to grant a tax credit for a cross-border dividend payment in certain circumstances. Thus, in paragraph 34, the Court accepted that “the situation of persons fully taxable in Finland might differ according to the place where they invested their capital. That would be the case in particular where the tax legislation of the Member State in which the investments were made already eliminated the risk of double taxation of company profits distributed in the form of dividends, by, for example, subjecting to corporation tax only such profits by the company concerned as were not distributed”.

In other words, the cross-border situation might be objectively different from a purely Finnish situation, in circumstances where the recipient of the dividend in Finland did not suffer economic double taxation. However, the Court pointed out that this situation did not exist in *Manninen*, since the Swedish company that paid the dividend was subject to corporation tax in Sweden on its corporate profits. Therefore, the Court held that the cross-border situation, in *Manninen*, was comparable to a domestic situation and Finnish shareholders that had invested in a Swedish company should be treated no less favourably under the national treatment principle.

The Court pointed out, in paragraph 46, that “the cohesion of that tax system is assured as long as the correlation between the tax advantage granted in favour of the shareholder and the tax due by way of corporation tax is maintained”.

126 See paragraphs 32-34 of the later *Meilicke II* case. *Wienand Meilicke and Others v Finanzamt Bonn-Innenstadt* (“*Meilicke II*”), C-262/09, ECLI:EU:C:2011:438. See also, *Mr and Mrs Robert Gilly v Directeur des services fiscaux du Bas-Rhin* (“*Gilly*”), C-336/96, ECLI:EU:C:1998:221, para. 48.

Host State

An example of a free movement of capital case, from a host Member State perspective, is seen in *Bouanich I*.¹²⁷

Bouanich I

Bouanich, a resident in France, held shares in a Swedish company. In 1998, the Swedish company repurchased its class B shares and made a payment to Bouanich. Under the Franco-Swedish DTC, withholding tax of 15% was payable in Sweden.

Bouanich argued that this tax treatment was less favourable than the tax treatment granted to a Swedish national who made a similar investment in that Swedish company and had his shares repurchased. That Swedish investor was entitled to deduct the acquisition cost of his shares and was taxed at 30% on the resulting capital gain. Bouanich was not granted this tax treatment. Instead, she was deemed to receive a dividend.

The Court noted that the right to deduct the acquisition costs of the shares was a tax advantage reserved for Swedish residents. The Court held that such legislation made “cross-frontier transfer of capital less attractive both by deterring investors who are not resident in Sweden from buying shares in companies resident in Sweden and also, consequently, by restricting the opportunities available to Swedish companies to raise capital from investors who are not resident in Sweden”.¹²⁸

The Court determined that Bouanich was in a comparable situation to a Swedish resident investor, pointing out, in paragraph 40, that “the cost of acquisition is directly linked to the payment made on the occasion of a share repurchase so that, in this regard, residents and non-residents are in a comparable situation. There is no objective difference between the two situations such as to justify different treatment on this point as between the two categories of taxpayers”.

Since Bouanich was in a comparable situation to a Swedish resident investor, she was entitled to national treatment in Sweden. However, there was a DTC in operation in this case which treated the payment to Bouanich as a deemed dividend, reduced the withholding tax rate to 15% but only allowed her to deduct the nominal value of the shares.

The Court stated, in paragraph 48, that it was necessary “to consider whether the Franco-Swedish agreement must be taken into account in determining whether tax legislation is consistent with Community rules on the free movement of capital. If that

127 *Margaretha Bouanich v Skatteverket (“Bouanich I”), C-265/04, ECLI:EU:C:2006:51.*

128 *Bouanich I*, para. 34.

is the case, it falls then to be established whether that agreement removes the restriction on fundamental freedom that has been found to exist". In other words, the Court had to investigate whether the DTC in this case eliminated or healed the potential restriction in this case.

Since it was impossible for the Court to determine whether the national treatment principle was breached, it returned the matter to the national referring court "to determine in the proceedings before it whether the fact that non-resident shareholders are permitted to deduct the nominal value and are liable to a maximum tax rate of 15% amounts to treatment that is no less favourable than that afforded to resident shareholders, who have the right to deduct the cost of acquisition and are taxed at a rate of 30%".

The outcome of *Bouanich I* is clear. Bouanich was entitled to no less favourable tax treatment in Sweden than a comparable Swedish investor. However, Bouanich could be treated under the DTC more favourably than the Swedish investor. The 15% tax rate would ensure a better result for Bouanich in a situation where the nominal value of the shares approximated the acquisition costs.¹²⁹ In such circumstances, the lower rate of tax under the DTC would ensure a better result than the 30% capital gains tax rate in Sweden.

The judgment in *Bouanich I* demonstrates that the Court is not applying a fiscal neutrality principle, but rather an equal treatment principle. The foreign investor could be treated more favourably under the Swedish domestic rules, when the DTC was taken into account. However, the Court's finding that Bouanich was in a comparable situation to a Swedish investor meant that she was entitled to national treatment or at least no less favourable tax treatment in Sweden.

Bouanich I also highlights how DTCs fit into the regulatory framework for tax in the EU. It is clear from *Bouanich I*, that DTCs may be used to eliminate a possible restriction in the source Member State.¹³⁰ The Court makes this clearer in its subsequent case law.

Amurta

Subsequently, the Court applied this reasoning in cases like *Amurta*.¹³¹ Since the DTC in question formed part of the legal framework to the case,¹³² the Court is bound to

129 This is an unlikely outcome given the litigation.

130 See Tom O'Shea, "Dividend Taxation Post-Manninen: Shifting Sands or Solid Foundations?" Tax Notes International, Mar. 5, 2007, 887-918, at p913; and Tom O'Shea, "EU Tax Law and Double Tax Conventions", (Avoir Fiscal, London, 2008), pages 54-55, where the author pointed this out for the first time in the literature.

131 *Amurta SGPS v Inspecteur van de Belastingdienst/Amsterdam ("Amurta")*, C-379/05, ECLI:EU:C:2007:655.

132 This was a matter for the national referring court to determine.

take it into consideration when giving guidance to the national court on EU law. Thus, in *Amurta*, the withholding tax on the outbound dividend amounted to a restriction on the free movement of capital because in a domestic setting the Netherlands did not impose a similar tax.

The Court explained, in paragraph 28, that “Treating dividends paid to companies established in another Member State less favourably than dividends paid to companies established in the Netherlands is liable to deter companies established in another Member State from investing in the Netherlands and thus constitutes a restriction on the free movement of capital prohibited, in principle, by Article 56 EC”.

The Court stressed that “as soon as a Member State, either unilaterally or by way of a convention, imposes a charge to income tax not only on resident shareholders but also on non-resident shareholders in respect of dividends which they receive from a resident company, the position of those non-resident shareholders becomes comparable to that of resident shareholders”.¹³³

Consequently, the Court concluded that “the Netherlands is under a duty to ensure that, under the procedures laid down by its national law to prevent or mitigate a series of liabilities to tax or economic double taxation, recipient companies established in another Member State are subject to the same treatment as recipient companies established in the Netherlands”.¹³⁴ This is an application of the national treatment test from a host Member State perspective.

The Court also stressed that “it cannot be excluded that a Member State may succeed in ensuring compliance with its obligations under the Treaty through the conclusion of a convention for the avoidance of double taxation with another Member State¹³⁵ ... (but) the Netherlands cannot rely on the existence of a tax advantage granted unilaterally by another Member State in order to escape its obligations under the Treaty”.¹³⁶

Accordingly, the Court concluded, in paragraph 83, that It was a matter for “the national court to establish whether account should be taken, in the main proceedings, of the DTC, and, if so, to determine whether that convention enables the effects of the restriction on the free movement of capital identified ... in paragraph 28 of this judgment, to be neutralised”.

133 *Amurta*, para. 38.

134 *Amurta*, para. 77.

135 *Amurta*, para. 79.

136 *Amurta*, para. 78.

Other areas of law

The national treatment principle has also featured in other areas of law beyond direct taxation. Some examples are clearly seen in relation to copyright law, EU Association Agreements and bilateral treaties concerning social security.

Copyright law

Phil Collins

In the landmark *Phil Collins* judgment,¹³⁷ the Court indicated that copyright and related rights fell within the scope of application of the Treaty because of their effects on intra-Community trade and consequently, “are necessarily subject to the general principle of non-discrimination laid down by the first paragraph of Article 7 of the Treaty...”¹³⁸

The Court explained that in prohibiting “any discrimination on grounds of nationality”, Article 7 of the Treaty (now Article 18 TFEU) “requires ...that persons in a situation governed by Community law be placed on a completely equal footing with nationals of the Member State concerned”.¹³⁹

Association Agreements

Sürül

The *Sürül* judgment¹⁴⁰ concerned an issue involving the EEC-Turkey Association Agreement.¹⁴¹ The Court held that a provision of that Agreement could have direct effect in the Member States, “when, regard being had to its wording and to the purpose and nature of the agreement itself, the provision contains a clear and precise obligation which is not subject in its implementation or effects, to the adoption of any subsequent measure”.¹⁴²

137 *Phil Collins v Imtrat Handelsgesellschaft mbH and Patricia Im- und Export Verwaltungsgesellschaft mbH and Leif Emanuel Kraul v EMI Electrola GmbH*. (“*Phil Collins*”) Joined Cases C-92/92 and C-326/92, ECLI:EU:C:1993:847.

138 *Phil Collins*, para. 27.

139 *Phil Collins*, para. 32.

140 *Sema Sürül v Bundesanstalt für Arbeit* (“*Sürül*”), C-262/96, ECLI:EU:C:1999:228.

141 EEC-Turkey Association Agreement available at – http://trade.ec.europa.eu/doclib/docs/2003/december/tradoc_115266.pdf (last accessed 17 January 2019).

142 *Sürül*, para. 60.

The Court commented that the “rule of equal treatment lays down a precise obligation of result and, by its nature, can be relied upon by an individual before a national court as a basis for requesting it to disapply the discriminatory provisions of the legislation of the Member State under which the grant of a right is subject to a provision not imposed on nationals. No further implementing measures are required”.¹⁴³

In support of its reasoning, the Court cited its settled case law¹⁴⁴ concerning Cooperation Agreements between the EEC and Algeria and Morocco, which the Court noted contained the principle of equal treatment in Articles 39(1) and 14(1) respectively of those agreements.

The Court explained that those provisions provided for “the prohibition of all discrimination based on nationality in the field of social security against Algerian and Moroccan nationals as compared with the nationals of the host Member State, are directly effective...”¹⁴⁵

For a more recent example, involving the EU-Tunisia and EU-Lebanon Association Agreements, see *SECIL - Companhia Geral de Cal e Cimento SA v Fazenda Pública*.¹⁴⁶ The Court applied the national treatment principle and held that “Legislation such as that at issue in the main proceedings, according to which a company which is a resident of a Member State may deduct in full or in part dividends from its taxable amount where the dividends are distributed by a company which is resident in the same Member State, but cannot make such a deduction where the distributing companies are resident in a third State constitutes a restriction on the movement of capital between Member States and non-member States which is, in principle, prohibited by Article 63 TFEU”.¹⁴⁷

Bilateral agreements

Gottardo

The *Gottardo* case¹⁴⁸ involved a bilateral social security agreement between a Member State and a non-member country that provided for account to be taken of periods of insurance completed in that non-member country for acquisition of entitlement to old-age benefits. The Court held that “the fundamental principle of

143 *Sürül*, para. 63.

144 Such as, *Zoubir Yousfi v Belgian State* (“*Yousfi*”), C-58/93, ECLI:EU:C:1994:160

145 *Sürül*, para. 66.

146 *SECIL - Companhia Geral de Cal e Cimento SA v Fazenda Pública* (“*SECIL*”), C-464/14, ECLI:EU:C:2016:896.

147 *SECIL*, para. 51.

148 *Elide Gottardo v Istituto nazionale della previdenza sociale (INPS)* (“*Gottardo*”), C-55/00, ECLI:EU:C:2002:16.

equal treatment requires that that Member State grant nationals of other Member States the same advantages which its own nationals enjoy under that convention unless it can provide objective justification for refusing to do so”.¹⁴⁹

Part III

National Treatment is not guaranteed in all cross-border situations

The Court has made it clear that the national treatment principle does not apply to all cross-border situations. This is particularly the case where the problem is caused by a disparity between the rules of two Member States rather than a restriction caused by the rules of a single Member State. Two landmark cases are *Lindfors*¹⁵⁰ and *Schempp*.¹⁵¹

Lindfors

In *Lindfors* (C-365/02), the Court accepted that sometimes the exercise of free movement rights could result in more burdensome tax treatment in the host Member State than that suffered in the origin State.

After many years residing in other Member States, Lindfors moved permanently to Finland and imported a private vehicle which she had purchased in the Netherlands. She was charged “autovero”, a vehicle registration tax, on this vehicle, which she challenged on grounds that it impeded her right of free movement.

While the Court accepted that the “autovero” tax was “capable of having a negative influence on decisions of citizens of the Union to exercise their right to freedom of movement as enshrined in particular by Article 18 EC”¹⁵² ... it pointed out that “the EC Treaty offers no guarantee to a citizen of the Union that transferring his activities to another Member State ... will be neutral as regards taxation. Given the disparities in the tax legislation of the Member States, such a tax advantage may be to the citizen’s advantage in terms of indirect taxation or not, according to circumstance. It follows that, in principle, any disadvantage by comparison with the situation in which that citizen carried on activities prior to that transfer is not contrary to Article 18 EC, provided that the legislation concerned does not place that citizen at a disadvantage as compared with those already subject to such a tax”.¹⁵³

149 *Gottardo*, para. 34.

150 *Marie Lindfors* (“*Lindfors*”), C-365/02, ECLI:EU:C:2004:449.

151 *Egon Schempp v Finanzamt München V* (“*Schempp*”), C-403/03, ECLI:EU:C:2005:446.

152 *Lindfors*, para.31.

153 *Lindfors*, para. 34.

This is important because it explains the scope of the national treatment principle which must be analysed from the perspective of the rules of either the host Member State or those of the origin Member State. Thus, if an EU citizen moves from the origin Member State to a host Member State where the tax rate is higher – this is not discrimination prevented by the national treatment principle from an origin Member State perspective.

Instead, the national treatment has to be applied from the perspective of the rules of the host Member State. Therefore, if the EU citizen moves to the host Member State and faces a rule which imposes a tax at a higher rate than a host State national, then that type of rule falls within the scope of the national treatment principle and may be prohibited by the fundamental freedoms and by the EU citizenship proviso contained in the TFEU. See, for example, *Schumacker*, discussed above.

Similarly, from an origin Member State perspective, the rule at issue must be an origin Member State rule which is causing a restriction or hindrance to the exercise of a fundamental freedom by an origin Member State national, when compared with the origin's Member State treatment of a comparable origin State national operating domestically. See, for example, *De Groot*, *Marks & Spencer* and *Keller Holding*, all discussed above

Schempp

A further example of this “two-State” problem in the direct tax field is seen in *Schempp*.

Schempp, who resided in Germany, paid maintenance payments to his former spouse who had moved to Austria. As a consequence, he no longer qualified for a tax deduction for the maintenance payments made to her because Austria did not tax such payments as income. Accordingly, under the German legislation at issue, the tax deduction was denied to *Schempp* in Germany. Had she moved to a Member State where such maintenance payments were taxed, he would have qualified for a tax deduction. *Schempp* argued that this was discriminatory.

The Court stressed that Article 12 EC (now Article 18 TFEU) had to be read in conjunction with the provisions of the Treaty concerning EU citizenship. It explained that Article 17(2) EC (now Article 20 TFEU) “attaches to the status of citizen of the Union the rights and duties laid down by the Treaty, including the right to rely on Article 12 EC in all situations falling within the scope of EU law”.¹⁵⁴

Those situations include the exercise of the fundamental freedoms and the EU citizenship right to move and reside in another Member State. By establishing her residence in Austria, *Schempp*'s former spouse exercised her free movement of EU

154 *Schempp*, para. 17.

citizenship rights. As a consequence, this was sufficient “to influence her former husband’s capacity to deduct the maintenance payments”.¹⁵⁵

The Court highlighted that “Article 12 EC is not concerned with any disparities in treatment ... which may result from divergences existing between the various Member States so long as they affect all persons subject to them in accordance with objective criteria and without regard to their nationality”.¹⁵⁶ Therefore, the Court explained that the payment of maintenance to someone living in Germany cannot be compared with the payment of maintenance to someone residing in Germany since “the recipient is subject in each of these two cases, as regards taxation of maintenance payments, to a different tax system”.¹⁵⁷

Since the situations were not comparable, there was no discrimination within the meaning of Article 12 EC.

The Court accepted that the transfer of residence by Schempp’s former spouse triggered unfavourable tax consequences for Schempp in his Member State of residence. However, the Court repeated its mantra that “the Treaty offers no guarantee to a citizen of the Union that transferring his activities ... will be neutral as regards taxation”.¹⁵⁸

The Court determined that this principle applied to Schempp’s situation even though he did not exercise his right of free movement.

Therefore, it is apparent from the Court’s jurisprudence that EU law does not preclude unfavourable consequences for free movement of workers that are the result of disparities between the rules of two or more Member States. Given the disparities between tax rates in the various Member States, a worker’s decision to rely on his or her freedom of movement can, depending on the circumstances, be more or less advantageous for such a worker from a tax perspective.¹⁵⁹

Deutsche Shell

The Court applied the same reasoning in the area of freedom of establishment. Thus, in *Deutsche Shell*,¹⁶⁰ the Court stressed that freedom of establishment “cannot be

155 *Schempp*, para. 24.

156 *Schempp*, para. 34.

157 *Schempp*, para. 35.

158 *Schempp*, para. 45.

159 See *Alphonse Eschenbrenner* (“*Eschenbrenner*”), C-496/15, ECLI:EU:C:2017:152, paras. 45 and 46.

160 *Deutsche Shell GmbH v Finanzamt für Großunternehmen in Hamburg* (“*Deutsche Shell*”), C-293/06, ECLI:EU:C:2008:129.

understood as meaning that a Member State is required to draw up its tax rules on the basis of those in another Member State in order to ensure, in all circumstances, taxation which removes any disparities arising from national tax rules, given that the decisions made by a company as to the establishment of commercial structures abroad may be to the company's advantage or not, according to circumstances".¹⁶¹

K case

Similarly, in relation to the free movement of capital, the Court has adopted the same approach.

In the *K case*,¹⁶² the Court determined that "a Member State cannot be required to take account, for the purposes of applying its tax law, of the possible adverse consequences arising from particularities of legislation of another Member State applicable to a property situated in the territory of that State which belongs to a resident in the first State ... The free movement of capital cannot be understood as meaning that a Member State is required to adjust its tax rules on the basis of those of another Member State in order to ensure, in all circumstances, taxation which removes any disparities arising from national tax rules, given that the decisions made by a taxpayer as to investment abroad may be to the taxpayer's advantage or not, according to circumstances".¹⁶³

Accordingly, in cross-border situations involving a disparity, national treatment may not be guaranteed since the problem is caused by the rules of two Member States rather than by the rules of a single Member State. In such circumstances, the hindrance to the exercise of a fundamental freedom does not constitute a restriction or discrimination prohibited by the fundamental freedom(s) at issue.

Part IV

Evolution of the EU's Direct Tax Jurisprudence

The EU's direct tax jurisprudence has not evolved in the way suggested by Schön. The restriction analysis did not magically appear after many years. It was always there from the outset in the Treaty of Rome.

161 *Deutsche Shell*, para. 43.

162 *K case*, C-322/11, ECLI:EU:C:2013:716.

163 *K case*, paras. 79 and 80.

Treaty of Rome

Article 3(c) of the Treaty of Rome (EEC) included among the activities of the Community the abolition, as between the Member States, of obstacles to freedom of movement for persons, services and capital.

Article 48(2) EEC, in relation to the free movement of workers, provided for the abolition of any discrimination based on nationality between workers of the Member States. Article 49 EEC provided that directives should be introduced to abolish a variety of restrictions provided for under national legislation or national administrative procedures and practices which formed an obstacle to the liberalisation of the free movement of workers. Article 52 EEC abolished restrictions on the freedom of establishment. Article 53 EEC prevented Member States from introducing new restrictions.

Article 59 EEC precluded restrictions on the freedom to provide (receive) services. Article 62 EEC prevented the Member States from introducing any new restrictions on the freedom to provide (receive) services. Article 67 EEC provided that Member States had to progressively abolish restrictions on the free movement of capital between Member States. Article 71 EEC prohibited Member States from introducing within the Community any new exchange restrictions on the free movement of capital.

It is clear from these provisions that the concept of restriction was in the Treaty of Rome from the outset. Whilst cases concerning discrimination against goods and persons came first, it is apparent from the above provisions that the Court could have discussed discrimination or restriction at any time depending on the cases that were brought before it. Indeed, in the direct tax area, the Court conducted a restriction and a discrimination analysis in *Avoir Fiscal*, in 1986,¹⁶⁴ many years before the *Kraus* judgment¹⁶⁵ mentioned by Professor Schön.

Avoir Fiscal

Avoir Fiscal was the Court's first "compliance" judgment concerning direct taxation.¹⁶⁶ The Court determined that the French rules at issue constituted a restriction on the exercise of freedom of establishment and discrimination on grounds of nationality. In other words, it concluded that the French rules at issue amounted to a discriminatory restriction. The Court stressed, in paragraph 14 of the judgment, that the freedom of establishment prohibits "as a restriction on the freedom of establishment, any discrimination on grounds of nationality resulting from the legislation of the Member State".

164 *Commission v France* ("*Avoir Fiscal*"), Case 270/83, ECLI:EU:C:1986:37.

165 *Dieter Kraus v Land Baden-Württemberg* ("*Kraus*"), C-19/92, ECLI:EU:C:1993:125.

166 As opposed to its first "competence" case, *Humblot*, from 1960. See *Jean Humblot v Kingdom of Belgium* ("*Humblot*"), Case C-6/60-IMM, ECLI:EU:C:1960:48.

Therefore, the French legislation at issue in *Avoir Fiscal* constituted a discriminatory restriction on grounds of nationality. As such, it could only be justified by a provision of the Treaty (and risk of tax avoidance was ruled out as a possible justification).¹⁶⁷

Futura

The Court's restriction discrimination and restriction approach became clearer in *Futura*,¹⁶⁸ where Luxembourg tax rules provided for loss carry-forward only if the losses were linked to the Luxembourg territory and a Luxembourg set of accounts was maintained for inspection in Luxembourg. The Court held that such tax rules were not discriminatory because they affected all persons (Luxembourg and non-Luxembourg) in a similar way. However, the Court determined that the requirement to maintain a second set of accounts for companies established in Luxembourg via branches amounted to a restriction in certain situations, that went beyond what was necessary under the principle of proportionality. In coming to this conclusion, the Court applied the reasoning adopted in its *Kraus* judgment.

Accordingly, the Court did not move from discrimination to restriction in its approach as suggested by many commentators. The Court simply dealt with the cases before it and continued to apply its discrimination and restriction analyses based on the circumstances of those individual tax cases and the arguments developed by counsel, by the intervening governments, by Advocates General and by the European Commission.

All discrimination, whether direct or indirect, constitutes a restriction, but all restrictions are not discriminatory. Plenty of non-discriminatory restrictions exist and have been discussed above. The main difference between discriminatory and non-discriminatory restrictions is in the way they can be justified. Unlike discriminatory restrictions, discussed above, non-discriminatory restrictions and indirect discrimination situations may be justified by the four pronged-formula set out in *Gebhard*.¹⁶⁹

167 See *Commission v Spain* ("Lotteries"), C-153/08, ECLI:EU:C:2009:618, para. 37, where the Court confirmed this reasoning: "to the extent that a restriction, such as that at issue in the present case, is discriminatory, it is compatible with Community law only if it is covered by an express derogating provision, such as Article 46 EC, to which Article 55 EC refers, namely public policy, public security or public health".

168 *Futura Participations SA and Singer v Administration des contributions* ("Futura"), C-250/95, ECLI:EU:C:1997:239.

169 *Reinhard Gebhard v Consiglio dell'Ordine degli Avvocati e Procuratori di Milano* ("Gebhard"), C-55/94, ECLI:EU:C:1995:411, para. 37. See also, *Dieter Kraus v Land Baden-Württemberg* ("Kraus"), C-19/92, ECLI:EU:C:1993:125, para. 32 and *Union royale belge des sociétés de football association ASBL v Jean-Marc Bosman, Royal club liégeois SA v Jean-Marc Bosman and others and Union des associations européennes de football (UEFA) v Jean-Marc Bosman* ("Bosman"), C-415/93, ECLI:EU:C:1995:463, para. 104, and *Commission v Germany*, Case 205/84, ECLI:EU:C:1986:463, para. 27 and earlier cited cases.

In paragraph 37, of *Gebhard*, the Court pointed out that “national measures liable to hinder or make less attractive the exercise of fundamental freedoms guaranteed by the Treaty must fulfil four conditions: they must be applied in a non-discriminatory manner; they must be justified by imperative requirements in the general interest; they must be suitable for securing the attainment of the objective which they pursue; and they must not go beyond what is necessary in order to attain it”.

The Court continues to deliver both discrimination and restriction judgments in the direct tax field and on occasion, judgments involving both a discrimination analysis and a restriction analysis as shown above.

Part V

Conclusions

Fiscal neutrality is not a general principle of EU law

The analysis conducted above demonstrates that the principle of fiscal neutrality is not a general principle of EU law. It is a more limited principle than the principle of equal treatment (or national treatment). It is not a “constitutional” principle like the principle of equal treatment but simply reflects the general principle of equal treatment in the areas of law where secondary EU legislation has been implemented, such as VAT, Parent-Subsidiary Directive and Mergers Directive, or where a specific rule of the TFEU requires it, like the internal taxation rule in relation to goods.

The Court has made it clear in its jurisprudence that fiscal neutrality contained in the various directives concerning tax is not unconditional. Indeed, failure to meet the conditions contained in the directive means that fiscal neutrality can be denied.

If fiscal neutrality existed as a general principle of EU law, it would be generally available in all cross-border situations involving the Member States and there would be no need to rely on the fiscal neutrality requirement contained in the directives.

Principle of Equal Treatment

It has been clearly demonstrated above that the principle of equal treatment is the defining principle operating in the Court’s direct tax jurisprudence. The unilateral neutrality test suggested by Professor Schön does not apply.

The inconsistencies with the concept of fiscal neutrality highlighted by Schön should ring enough alarm bells to suggest that maybe he is wrong and that the Court is doing things in a different way to the fiscal neutrality approach suggested by him and a number of other commentators.

This failure to understand the principle of equal treatment permeates the rest of his criticisms of the Court's direct tax jurisprudence. Schön criticises the Court concerning the *Schumacker* line of cases, the *Manninen* line of cases, the *Marks & Spencer* line of cases, the *Amurta* line of cases and the Court's approach to the taxation of dividends.

All of these cases have been discussed above and Schön's criticisms of the Court have been shown to be unfounded. If the principle of equal treatment is applied to any or all of these cases, as outlined above, the Court's direct tax cases fit together in a consistent way as one would expect.

Finally, this analysis has demonstrated the need for a review of the scholarly literature concerning the principle of fiscal neutrality.