

When taxing a non-residents income, a source state does not have to grant tax correctives on account of civil status or family responsibilities, applicable for its own residents, unless the income is the almost exclusive taxable income of the non-resident. This so-called 'Schumacker-principle', although dating from 1995, still raises questions. This article critically analyzes the judgment of the Court of Justice in the Kieback-case, where the Court had to decide about its application for the deduction of costs, linked to a foreign immovable property, in case of a non-resident earning all his taxable income during a part of a tax year in the source state and then moving to a third State. The court insisted that the Schumacker-principle can include costs which, according to the tax legislation of the source state, are in particular linked to foreign income, the possibility of discrimination has to be considered exclusively from a tax perspective, but the comparison can be made taking into account an entire tax year. Based on these premises the Court concluded that the foreign negative income did not have to be taken into account in the source state.

## ***Kieback: when Schumacker emigrates ...***

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### ***Introduction***

On 18 June 2015 the Court of Justice delivered a preliminary ruling, where it refused a requested hearing, deviated from the opinion of its Advocate General Sharpston, as well as from the expressed opinions of all domestic courts having pronounced earlier on the particular case.

The judgment concerned the case of M. Kieback, a resident of Germany, who moved from Germany to the U.S. during a particular tax year. When living in Germany he worked for a Dutch hospital and earned most of his taxable income from the Netherlands. During this period he owned his own dwelling and paid mortgage interest for a loan agreement. After three months he moved from Germany to the US, ended up his employment in the Netherlands and started working for an American employer.

A few months later he sold his German house and (presumably) cleared the mortgage.

Mr. Kieback deducted his German mortgage interest supported during the period he was working in the Netherlands from his Dutch taxable income, which was refused by the Netherlands tax administration.<sup>2</sup> He successfully challenged the administrative view for the lower District Court<sup>3</sup>, whose judgment was confirmed by the Court of Appeal<sup>4</sup>. The tax administration continued the proceedings for the Dutch Hoge Raad. In his conclusions for the Hoge Raad, the Dutch Advocate-General also followed the point of view of the taxpayer, but nonetheless advised to request for a preliminary ruling.<sup>5</sup> The Hoge Raad concurred.

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<sup>2</sup> Although according to the applicable Dutch tax legislation, Mr. Kieback could opt to be treated as a Dutch resident, he did not choose to, but claimed the deduction being treated as a non-resident.

<sup>3</sup> Court of first instance of Breda 6 July 2011, nr. AWB 09/1465.

<sup>4</sup> Court of Appeal 's Hertogenbosch 23 March 2012, nr. 11/00567, NTFR 2012, 1019.

<sup>5</sup> ECLI:NL:PHR:2013:BZ6237.

After summarizing potential interpretations and expressing its favor for granting the requested deduction, the Hoge Raad referred two questions for a preliminary ruling to the European Court of Justice.

The main question concerns the interpretation of art. 39 EC-treaty (art. 45 TFEU). Does this article demand from a Member state X where a resident y of another Member State Y is employed to take into account the personal and family circumstances of this non-resident, when taxing his employment income, in case the employment is only exercised for a part of the tax year, but forms the main source of income for the employee during this period? As after this period the employee y emigrates from his home state Y to another home state Z, the home state Y itself is not able to take into account the personal and family circumstances of y. However, when focusing on the entire tax year, the salary this person obtained in the source state X is not almost all of his income.

The requesting Court further wonders whether it would make any difference if the second home State (Z) were a Member State of the European Union or a third state.

The Court of Justice concluded that art. 39 EC-treaty does not oblige the Member State X, when taxing the income of a non-resident worker y, to take into account the personal and family circumstances of this person, when the income is the main income of the non-resident during a part of a tax year, but not for a complete tax year. It does not make any difference whether this person moves to another Member State of the EU or to a third state.

This decision will be critically analyzed in this article, based on previous judgments of the Court of Justice. First the basic principles of the Court's reasoning coming from the well-known Schumacker-case will shortly be repeated. In a second step the interpretation of 'discrimination' as it follows from the Court's reasoning will be questioned in this case from three particular angles. From earlier judgments it follows that a source state has to take into account deductions closely linked with foreign income, and the possible existence of a discrimination is determined from an all-or-nothing approach towards one state. Although these both point of views are open to criticism the Court held on to its point of view. Finally, the Court's conclusion on the timing issue differed from all earlier expressed opinions in this particular case and does not convince the author of this article.

As only the first question concerns the general principle, the second question will not be dealt with separately.

### ***Free movement of workers: ban on discriminations of foreign workers***

As a first step it can be stressed that the European regulation concerning free movement of workers is not primarily focused on an equitable tax treatment in itself. In national income taxation, the taking into account of the ability to pay when calculating the taxes due, and in application thereof offering particular personal allowances, is generally seen as a basic principle in search for an equitable calculation of the taxes due.

The free movement of workers however implies the verification of "*the abolition of any discrimination based on nationality between workers of the Member States as regards employment, remuneration and other conditions of work and employment*". This equality of

treatment has to be ensured in fact and in law.<sup>6</sup> The Court of Justice concluded that not only overt discriminations on nationality, but also covert forms of discrimination which, through the application of other criteria of differentiation, lead in fact to the same result are forbidden. An obvious criterion in this aspect would be 'residence'.<sup>7</sup>

However, as it comes to direct taxation, a different treatment based on residency is in general not considered to be discriminatory. When taxing a non-resident's (y) income a state's (X) taxing competence is based on the link between taxable income and the territory over which it exercises its taxing power. The taxing competence is determined *ratione materiae*, without considering particularities of the tax payer (y) as such. When taxing its own residents (x) a State's (X) taxing competence is based on the link between the tax payer and the territory of a state. The taxing competence is determined *ratione personae*. This generally justifies why, when taxing residents, often the worldwide income will be taken into account and non-residents are only imposed on the source income. Consequently the taxation of both categories can and will differ. The calculation of the particular income in the state of source needs to be comparable for non-residents and residents, but relief or deductions that are not linked to the taxable income as such can differ for both categories.<sup>8</sup> Illustrative in this context is art. 24, 3 of the OECD Model Tax Convention. It explicitly mentions that the provision on non-discrimination "*shall not be construed as obliging a Contracting State (X) to grant to residents of the other Contracting State (Y) any personal allowances, reliefs and reductions for taxation purposes on account of civil status or family responsibilities which it grants to its own residents*". The OECD Commentary explains that the purpose of this exclusion is to avoid non-residents being treated better, as they would receive personal allowances and reliefs for family responsibilities in both states. However, the commentary explicitly mentions the option for a source state to offer these reliefs *in the proportion which the amount of the source profits bears to the world income in the other State*.<sup>9</sup>

In the EU this particular concept of non-discrimination has been further elaborated in the well-known and often cited Schumacker-case.<sup>10</sup> According to the Court, art. 45 TFEU precludes "*the application of rules of a Member State (X) under which a worker (y) who ... resides in another Member State (Y) and is employed in the first State (X) is taxed more heavily than a worker (x) who resides in the first State and performs the same work there when ... the national (=resident y) of the second State obtains his income entirely or almost exclusively from the work performed in the first State and does not receive in the second*

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<sup>6</sup> Fifth consideration of Regulation (EEC) No 1612/68 of the Council of 15 October 1968 on freedom of movement for workers within the Community (*OJ L 257*, 19 October 1968), being replaced by Sixth consideration of Regulation (EU) No 492/2011 of the European Parliament and of the Council on freedom of movement for workers within the Union (*OJ L 141/1*, 27 Mai 2011).

<sup>7</sup> CJCE 12 February 1974, C-152/73, Sotgiu, [www.curia.eu](http://www.curia.eu). Earlier however, in the case Ugliola, the Court already prohibited Member states to distinguish *by indirectly introducing discrimination* in favor of their own nationals alone based upon obligations for military service. (The difference between military service exercised in Germany, which was added for the calculation of the term of office for a German employer, and service exercised elsewhere was not accepted.) Cf. CJCE 15 October 1969, C-15/69, Ugliola, [www.curia.eu](http://www.curia.eu).

<sup>8</sup> CJCE 5 July 2005, C-376/03, D., [www.curia.eu](http://www.curia.eu).

<sup>9</sup> §36 OECD Commentary on art. 24. The Belgian double tax conventions with France (art. 25, §2 Conv.) and the Netherlands (art. 26, §2 Conv) provide a pro rata for natural persons; while the Belgian convention with Luxembourg provides this only for residents of Luxembourg earning income in Belgian. (art. 24, §4b Conv.).

<sup>10</sup> CJCE 14 February 1995, C-279/93, Schumacker, [www.curia.eu](http://www.curia.eu).

*State sufficient income to be subject to taxation there in a manner enabling his personal and family circumstances to be taken into account”.*<sup>11</sup>

In this case the Belgian resident, Mr. Schumacker, started working in Germany from 15 May 1988 until 31 December 1989. Before, he was employed in Belgium and during 1988 his wife also drew unemployment benefit support in Belgium<sup>12</sup>. It was only since 1989 that Mr. Schumacker’s wages have been the household’s sole income. Nonetheless, (already) on 6 March 1989 he asked the German tax administration to offer him the tax advantages accorded to residents.

More in particular the advantages concerned *a.o.* the splitting of income (the total income of a German couple would be aggregated, attributed to each spouse for 50 % and taxed accordingly), as well as the taking into account of personal and family circumstances giving rise to tax reliefs and rebates.

The German Finanzamt refused to calculate the income tax of Mr. Schumacker ‘*on an equitable basis*’<sup>13</sup> by decision of 22 June 1989. On this date there was still no entire tax year Schumacker had been earning his households only taxable income. It was only in the subsequent procedure one could focus on an entire tax year (1989) compared to a shorter period in 1988. However, in its prejudicial questions, referring the case to the Court of Justice in 1993, the Bundesfinanzhof did not make this distinction. It only referred to the general case of a person (y) earning almost all of his income in a particular source state (X). Therefore, in its ruling, the Court of Justice concluded with the general observation that “*a discrimination arises from the fact that his personal and family circumstances are taken into account neither in the State of residence nor in the State of employment*”.<sup>14</sup>

In the Wielockx-case the Court applied the same principle for independent workers.<sup>15</sup> Finally, this principle has been extended in application of the Agreement between the European Community and its Member States, of the one part, and the Swiss Confederation, of the other, on the free movement of persons.<sup>16</sup> After the Swiss Supreme Court applied the Schumacker-doctrine in case of the Swiss (X) withholding tax on a French resident (y) working as an independent in Switzerland<sup>17</sup>, the Court of Justice did the same for German independent workers moving their residence from Germany to Switzerland (Y) but

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<sup>11</sup> §47.

<sup>12</sup> In the case Gschwind the court explicitly confirms that the combined income of the household can be taken into account. (Cf. CJCE 14 September 1999, C-391/97, Gschwind, [www.curia.eu](http://www.curia.eu).) Nonetheless, from the case of Wallentin it can be concluded that ‘non-taxable income’ does not have to be taken into account. (CJCE 1 July 2004, C-169/03, Wallentin, [www.curia.eu](http://www.curia.eu)) Belgium, however, does consider payments for unemployment as taxable income, but provides for a particular technical deduction to guarantee an exemption. Nonetheless, as personal allowances are first held against this income, it seems reasonable to take it into account.

<sup>13</sup> The formulation in § 163 of the German tax Code when offering the right to split the income over a married couple.

<sup>14</sup> §38.

<sup>15</sup> CJCE 11 August 1995, C-80/94, Wielockx, [www.curia.eu](http://www.curia.eu). This case concerned a Belgian resident, working a whole year in the Netherlands and earning all of his income in the source state. The Court’s similar judgment was consequently not surprising.

<sup>16</sup> Agreement of 21 June 1999, OJ L 114, 30 April 2002.

<sup>17</sup> Swiss Supreme Court 26 January 2010, Joined Cases 2C.319/2009 and 2C.321/2009. The case concerned the refusal of deduction of professional cost, directly linked to the Swiss income, as well as general commuting costs and expenses for pension fund contributions creating a tax deduction for Swiss residents. Cf. R. HEUBERGER and S. OESTERHELT, “Swiss Salary Withholding Tax Violates Free Movement of Persons Agreement with the European Union”, *E.T.* 2010, nr. 7, 285-294.

continuing their professional activities in Germany (X).<sup>18</sup>

The outcome of these decisions, interpreting the free movement of workers, generally can be summarized as the right for a foreign worker (y) to be treated equally as a national.<sup>19</sup> Criteria based on residence can cause a covert discrimination and are submitted to the same commitment of non-discrimination. Once persons are in the same situation the taxation of their income has to be equal. If, for a person working abroad, his personal and family circumstances are nowhere taken into account, a discrimination arises, which can only be tolerated if there is a justification.

### ***What is discrimination ?***

In general, discrimination concerns similar situations being treated differently or different situations being treated equally without any acceptable justification.<sup>20</sup> Although the equalization in a source state X of residents and non-residents for direct income taxes under the Schumacker-case already dates from 1995, the precise scope of this principle still raises many doubts and certain points of view are still heavily criticized. In this analysis the focus will be on the different correctives that have to be taken into account, the general (but nonetheless limited to tax effects) approach of the Court and the influence of time periods differing from a standard tax year.

### **Which tax correctives have to be taken into account ?**

Tax correctives exist in very different forms, including deductible expenses, particular deductions, allowances, ... It seems not immediately possible to make a general distinction or terminology applied in all Member states. Nonetheless, a first deduction could be made between tax rules related to the taxation of the 'foreign' income itself, income-related corrections, and more general tax allowances or deductions.

As far as the taxation of the income itself is concerned, the source state (X) always has to take into account for non-residents, as well as for residents, all factors that are linked to this income for the determination of the taxable base and the taxes due. Concerning the determination of taxable income earned in a source state (X), residents and non-residents are generally considered to be in a similar situation. This can rather easily be determined for deductible costs linked to taxable income<sup>21</sup>, a tax rate on income<sup>22</sup> or domestic procedures

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<sup>18</sup> CJCE 28 February 2013, C-425/11, K. Ettwein, [www.curia.eu](http://www.curia.eu).

<sup>19</sup> However, in a recent judgment the Court repeated that nationality can be used as a criterion to distinguish in the tax treatment, if nationality is the criterion to apportion taxing competences. Cf. CJCE 19 November 2015, C-241/14, R. Bukovansky, [www.curia.eu](http://www.curia.eu).

<sup>20</sup> For a more profound search for a definition to be integrated in a provision, see B. SANTIAGO, "Non-Discrimination Provisions at the Intersection of EC and International Tax Law", *E.T.* 2009, 249-262.

<sup>21</sup> Cf. CJCE 12 June 2003, C-234/01, Gerritse; CJCE 3 October 2006, C-290/06, FKP Scorpio Konzertproduktionen GmbH; CJCE 15 February 2007, C-345/04, Centro Equestre de Leiria Grande L<sup>de</sup>; CJCE 31 maart 2011, C-450/09, Ulrich Schröder; CJCE 8 November 2012, C-342/10, Commission v. Finland, [www.curia.eu](http://www.curia.eu).

The case of Gielen considered a particular reduction for the taxation of business income in the Netherlands. Although this deduction was not based on specific costs, nonetheless the Court accepted the link with the business income and demanded, in line with this cited judgments, a similar treatment for non-residents and

the tax payer has to respect<sup>23</sup>. However, recent case law concerning other freedoms shows that the determination of the factors that have to be taken into account, can also demand a more comprehensive analysis. E.g. the Court accepted that expenditures for advice for the tax declaration in the source state (X) should be deductible under the same circumstances for non-residents, as for residents, if these costs only cover the declaration of the taxable income in this state.<sup>24</sup> The Court also considered several times that, even though for a particular income the same withholding tax applies, nonetheless, based on the overall tax regime for residents, they unjustifiably benefitted from a more advantageous taxation.<sup>25</sup> As this question is not at stake in the Kieback judgment, this will not further be elaborated. However, the judgments are cited to illustrate that, although comparing the tax treatment of a resident and a non-resident receiving a particular taxable income requires an analysis of a specific item of taxable income, the Court is nonetheless willing to investigate from a more comprehensive approach.

As far as general tax allowances or deductions are concerned, this seems to be a broad category covering allowances based on personal and family circumstances, as well as deductions not linked to a particular income.<sup>26</sup> As the Court only expressed itself in particular case law on specific expenditures or allowances, it is rather difficult to exhaustively determine which tax correctives do apply for this category.

A standard exemption for a tax free minimum income, an additional deduction for children at charge, the possibility of splitting income over a household or a deduction of alimony payments all seem rather clear examples of deductions at stake. But what to think of more general tax reductions for social stimuli, to encourage long term savings, a private pension accrual, investments in amelioration of private housing ? These could also be tax stimuli accorded to improve a persons living standard and are not linked to a particular taxable income either.<sup>27</sup>

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residents earning such business income in the source state (= the Netherlands). Cf. CJCE 18 March 2010, C-440/08, Gielen, [www.curia.eu](http://www.curia.eu).

<sup>22</sup> Cf. CJCE 27 June 1996, C-107/94, Asscher; CJCE 6 October 2009, C-562/07, Commission v. Spain, [www.curia.eu](http://www.curia.eu). (Not accepting a higher tax rate for non-residents on income, although because of the progressive taxation of residents one could consider the non-resident being favored). The same has been ruled for corporations. Cf. CJCE 29 April 1999, C-311/97, Royal Bank of Scotland and CJCE 23 February 2006, C-253/03, CLT-UFA, [www.curia.eu](http://www.curia.eu). However, in a recent judgment, the Court accepted a lower tax rate for non-residents combined with the exclusion of all possible deductions, whereby the source state (Sweden) left the possibility for non-residents to opt in general for a tax treatment as a resident. Cf. CJCE 19 November 2015, C-632/13, H. Hirvonen, [www.curia.eu](http://www.curia.eu).

<sup>23</sup> Cf. CJCE 15 September 1998, C-231/96, EDIS; CJCE 15 September 1998, 279/96, Ansaldo Energia a.o.; CJCE 2 October 2003, C-147/01, Weber's Wine World.

<sup>24</sup> Cf. CJCE 6 July 2006, C-346/04, R.H. Conijn, [www.curia.eu](http://www.curia.eu).

<sup>25</sup> Cf. CJCE 20 October 2011, C-284/09, Comm. v. Germany; CJCE 12 July 2012, C-384/11, Tate & Lyle Investments Ltd; CJCE 25 October 2012, C-387/11, Commission v. Belgium and CJCE 17 September 2015, C-10/14, C-14/14 and C-17/14, J.B.G.T. Miljoen a.o., [www.curia.eu](http://www.curia.eu). All these cases have in common that only for non-residents the withholding tax would be a definitive taxation. For residents the calculation of the taxable income is influenced by other legal corrections, while the withholding tax is credited against the final tax.

<sup>26</sup> Schön distinguishes between expenditures linked to taxable income and general business expenditures. Cf. J. SCHON, "Neutrality and Territoriality – Competing or Converging Concepts in European Tax Law?", *B.I.T.* 2015, 285-286.

<sup>27</sup> Illustrative in this 'linking context' is the evolution of the Court from its judgments in 1992 (CJCE 28 January 1992, C-204/90, Bachmann and C-300/90, Commission v. Belgium, [www.curia.eu](http://www.curia.eu)) towards later judgments (CJCE 3 October 2002, C-136/00, Danner; CJCE 30 January 2007, C-150/04, Commission v. Denmark; CJCE 5 July 2007, C-522/04, Commission v. Belgium). Whereas in the beginning a kind of cohesion between the (deduction



It is tempting to refer to all kind of tax favours based on a tax payers 'ability to pay tax'<sup>28</sup>, when looking for a common denominator of these tax correctives. However, besides the fact that this notion in itself is unclear, this is not the European concern. A potential restriction of the free movement of workers has to be judged based on a discrimination analysis. In addition, one has to notice that some of the tax favours at stake will be deducted from a persons globalized taxable income. In case of a progressive income tax rate therefore the effect of these deductions will rise as the taxable income raises. Such measures seem the adverse of measures taking into account a person's ability to pay tax.<sup>29</sup>

In his opinion on the Lakebrink-case, Advocate-General Mengozzi supports the view that in case a non-resident (y) earns (almost) all of his taxable income in the source state (X), he should be considered as a resident *"not only as regards the grant of tax benefits linked to the non-resident's personal and family circumstances, but also in relation to any aspect of his overall ability to pay which is relevant for according tax benefits to residents"*.<sup>30</sup>

This view cannot be supported either. The ability to pay taxes is in fact determined by all the income of a person, being a combination of his profits and losses. As losses of a professional activity do influence the ability to tax, they can be deducted from taxable income of a tax payer. Therefore a home state (Y) often offers the possibility to deduct foreign losses from a tax payer's taxable income, although foreign positive income would have been exempted. Kemmeren already pointed out correctly that it would not be in line with the European jurisprudence, neither with the balanced allocation of tax jurisdiction between Member States based on DTC's to oblige a source state (X) to also take into account all of this negative income aspects.<sup>31</sup>

First of all, even a home state cannot be obliged to take into account foreign losses when calculating the taxable income of its residents. If the foreign positive income is tax exempt, the home state could accept to exclude it completely (positive, as well as negative) from calculating domestic taxes.<sup>32</sup> But additionally, even if a home state (X) does take into account negative income from outside its territory, when taxing its residents (x), this situation fundamentally differs from the situation of a non-resident (y) earning (almost) all of his taxable income in this state. Although, when taxing its residents (x), state X possibly exempts foreign (positive) income in other taxable years, this (positive) income might be taken into account for a so-called progression reservation, to consider the tax rate applicable for the taxable income. Besides, in most cases this state will also integrate a kind of clawback system. If a foreign loss, taken into account in the home state, will in a later taxable period also be taken into account in the source state, the home state will reintegrate the previously

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of the) payments and the (taxation of the) capital was accepted, the Court did no longer consider this link to exist (or accepted that Member States broke it up themselves with the conclusion of a double tax convention).

<sup>28</sup> Cf. CJCE 18 July 2007, C-182/06, Lakebrink, §34. Mattsson qualifies these measures as corrections on the tax rate instead of corrections on the tax base. Cf. N. MATSSON, "Does the European Court of Justice Understand the Policy behind Tax Benefits Based on Personal and Family Circumstances?", *E.T.* 2003, 193.

<sup>29</sup> This is why in a pure domestic context, when a legislator expressly wants to focus on a person's ability to pay tax and provides additional corrections besides a progressive tax rate, preference should be given to correctives calculated on a flat rate or taking effect on the lowest tax rates.

<sup>30</sup> Concl. Mengozzi, 29 March 2007, C-182/06, Lakebrink, §36. It seems to be the same logic that drove this person towards his conclusion in the Renneberg-case. (Conclusion of 9 July 2008, C-527/06).

<sup>31</sup> E. KEMMEREN, "Renneberg Endangers the Double Tax Convention System or Can a Second Round Bring Recovery ?", *EC Tax review* 2009, nr. 1, 10.

<sup>32</sup> Cf. CJCE 7 November 2013, C-322/11, K., [www.curia.eu](http://www.curia.eu).

deducted losses in the taxable base. Finally, even if the home state does not apply such claw back systems, at least, based on the generally applied allocation of tax jurisdictions, it has the possibility to integrate this into its tax system when taxing its residents, whereas a mere source state taxing a non-resident hasn't. Therefore a non-resident y, earning all of his positive income in a source state X, and only losses in other states, is not in an entirely similar situation as residents of this state X. Even if this difference would not be taken into consideration when verifying whether a restriction on the free movement exists, at least the territoriality-principle and the balanced allocation of tax jurisdiction between Member States would justify that foreign losses are only taken into account when taxing residents and not for the taxation of non-residents, even though they would earn almost all of their income in this state.

Although one could defend that a source state X takes into account the personal situation of y when calculating the taxes due, the scope of these deductions therefore has to be limited, which still causes a taxable base differing from a resident's taxable base.

Therefore, the question remains, which tax corrections a source state X should take into account, when a non-resident y earns almost all of his taxable income in this state. As already illustrated, for income-related tax corrections the source state X always has to treat non-residents and residents equally. Conversely, it can be argued that this source state X does not have to apply its domestic tax corrections linked to foreign income when taxing a non-resident y on his income earned in X. This holds true, even if y earns almost all of his taxable income in X. In this last case, it would seem acceptable that all non-income-related tax corrections have to be taken into account. These can be person-related tax corrections<sup>33</sup>, as well as tax incentives given as a financial incentive to pursue a specific non-fiscal purpose.<sup>34</sup> One could conclude that all corrections that are not particularly linked to a (foreign) specific income need to be taken into account by the source state (X).<sup>35</sup> This can only be limited to investments/expenses located on the territory of the source state X, if such limitation also applies for its own residents (x) and is in itself considered to be EU-conform.

Who will determine whether a particular tax correction is related to specific taxable income, linked to a person's situation or focused on a particular non-fiscal purpose ?

In a comparable situation, Wiemann refers to earlier judgments of the Court<sup>36</sup> to conclude that such qualification is an autonomous qualification of European law, to be determined by

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<sup>33</sup> In the double tax treaty between Belgium and the Netherlands the source state gives the same tax correctives ('*persoonlijke aftrekken, tegemoetkomingen en verminderingen*') "*uit hoofde van burgerlijke staat of samenstelling van het gezin*" (based on civil status or constitution of the household) as residents. (art. 26, §2 Convention) In a judgment of 2010 the Dutch Hoge Raad considered that tax corrections for aged people (*ouderentoeslag en ouderenkorting*) do not fall under this category. Cf. H.R. 19 February 2010, nr. 08/02184, NTFR 2010, 542 note PETERS. This shows that also this notion is rather unclear.

<sup>34</sup> Cf. J. WIEMANN, "Deductibility of Health Insurance and Social Security Contributions", EC Tax Review 2011, 2, 98.

<sup>35</sup> Compare with Schön who reads in recent jurisprudence of the Court of Justice a subsidiary obligation for the Member State to take into account deductions that cannot be used in the source Member State. Cf. W. SCHON, "Neutrality and Territoriality – Competing or Converging Concepts in European Tax Law?", *B.I.T.* 2015, 275.

<sup>36</sup> In C-209/01 (Schilling) the Court implicitly qualified a German deduction for expenses for a household worker as a person-related tax correction. In the already mentioned case C-346/04 (Conijn) the Court qualified costs for a tax declaration as expenses linked to the declared income.



the Court of Justice.<sup>37</sup> However, there is no guiding (European) legislation using these terms and the notions are neither defined yet in the European jurisprudence. In addition, it seems that a large scale of possibly very different tax corrections are imaginable, depending on the autonomous tax policy of a Member State. When classifying, the Court therefore should at least dispose of an extensive explanation how a particular tax correction fits within the income tax system of a Member state. Even if a particular tax correction seems at first sight similar in different Member States, it can be integrated throughout a completely different policy.

The difficulty to qualify a particular correction can be illustrated with the (tax) correction integrated in Member states' tax legislations to stimulate the acquisition of immovable property, as this was also at stake in the commented case. This correction is often linked to the payments (in many cases interests, as well as capital repayments) for a mortgage loan.<sup>38</sup> The technical integration in a domestic tax system can however differ and cause a different qualification.

The basic aim to support people investing in immovable property can be explained as a deduction of the cost to generate taxable income: immovable property generates taxable income<sup>39</sup> and therefore the costs to acquire this income should be deductible. Even if an extensive correction is provided - not only deducting the real (interest) cost, but also the capital repayments - this correction could be considered to be linked to the taxable income in the state where the immovable property is located.

However, stimulating the investment in someone's own dwelling also bears a social component. It offers a financial certainty, can be seen as a private pension accrual, and guarantees someone's living standard. The Belgian tax regime therefore offers a particular reduction for the mortgage payments, which can be imputed on the total of taxes due.<sup>40</sup> The amount of this reduction is up to a fixed amount<sup>41</sup>, which is a.o. raised the first 10 years of the mortgage, as well as for persons having at least 3 children at charge. In case of a married couple living together, each of the partners receives the full lump sum reduction. Although living in the building is a condition for the reduction and the amount of the reduction can be reduced in some cases if a person acquires a second immovable property, this tax reduction is not linked to (any taxable income that could be generated from) this immovable property. It rather seems a personal allowance. This system is not applicable for additional immovable properties. For additional mortgage payments a less advantageous tax system exists, that nonetheless also takes into account interest costs as well as capital repayments.<sup>42</sup>

The tax correction offered for mortgage payments can therefore be an income-related, as well as a person-related corrective. This has troubled earlier jurisprudence and raised criticism against the position taken by the Court, as will be illustrated with some cases.

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<sup>37</sup> Cf. J. WIEMANN, "Deductibility of Health Insurance and Social Security Contributions", EC Tax Review 2011, 2, 98.

<sup>38</sup> Only these payments will be analyzed. Negative income caused by amortizations will not further be taken into account. (E.g. CJCE 15 October 2009, C-35/08, Grundstücksgemeinschaft Busley, [www.curia.eu](http://www.curia.eu).)

<sup>39</sup> In case of a person's private dwelling a fictitious income often will be integrated.

<sup>40</sup> Art. 145/37 and following Belgian Income Tax Code (B.I.T.C.).

<sup>41</sup> This amount is probably lower than the total of mortgage payments during a taxable year. If however payments are lower (e.g. the year the loan starts or ends) only the total of payments will be taken into account for a reduction.

<sup>42</sup> Art. 145/1, 3° B.I.T.C.

In its first judgments, concerning taxation in the source state X, the Court did not conclude firmly on the qualification of this tax correction.

A first judgment, worth mentioning, is the Ritter-Coulais-case.<sup>43</sup> It concerned a German couple living in France (Y), but working in Germany and being taxed on their total income in Germany (X). Germany, as a source state X, refused to take into account the negative income from their French dwelling, although foreign positive income from immovable property would be taken into account to determine the applicable tax rate. In the preliminary procedure the Court was asked whether the exclusion of foreign ‘negative income’<sup>44</sup> violated the European freedom.<sup>45</sup> Although the referring German Court seemed to consider the tax correction to be linked with immovable income, this did not determine the outcome of the case.<sup>46</sup> The Court simply referred to the taking into account of positive foreign income. As a resident (x) can deduct its domestic negative income, persons residing outside Germany are being discriminated. If a source state (X) takes into account foreign positive income, there is no longer a justification to distinguish between residents and non-residents as far as negative income from their personal housing is concerned. The German exclusion was considered to violate the free movement of workers.

In the Lakebrink-case<sup>47</sup> the discrimination was less obvious. The case concerned a German couple, living in Germany (Y), but working exclusively in Luxembourg (X). When taxing their income in Luxembourg, the Luxembourg tax administration refused to take into account foreign ‘negative income’, determined according to *German* tax legislation. The couple owned two immovable properties in Germany, they did not occupy themselves. In a German tax declaration this was declared as ‘negative income’. The Luxembourg tax administration refused a deduction to determine the tax rate for the Luxembourg taxable income, because also positive (non-professional) income would have been excluded when calculating the applicable tax rate for non-residents.

Again the question for a preliminary ruling clearly linked ‘the deduction’ with the particular property situated in Germany and additionally even explicitly mentioned that it was not occupied by the couple. Although the Court accepted the qualification of ‘*rental income losses from properties*’<sup>48</sup>, it subsequently continued its reasoning, based on the Schumacker-principle. The Court based its opinion on a general notion of ‘negative income’. The discrimination of non-residents (y) concerns “*all the tax advantages connected with the non-resident’s ability to pay tax which are not taken into account either in the State of residence or in the State of employment ... since the ability to pay tax may indeed be regarded as forming part of the personal situation of the non-resident*”.<sup>49</sup> This seems to follow the reasoning in the Opinion of the advocate-general, as already criticized.

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<sup>43</sup> CJCE 21 February 2006, C-152/03, Ritter-Coulais, [www.curia.eu](http://www.curia.eu).

<sup>44</sup> The precise scope of ‘negative income’ is not clarified in the judgment. The advocate-general mentions that this can originate from the personal use of immovable property. Cf. Concl. Léger, C-152/03, §10.

<sup>45</sup> The referring judge asked the Court about the conformity with the freedom of establishment and the free movement of capital. The Court however reconsidered the case and challenged the regulation under the free movement of workers.

<sup>46</sup> In his opinion in the case Renneberg Advocate-General concludes from this omission that negative income might be different from personal circumstances. Cf. Concl. Mengozzi, C-527/06, §47 and following.

<sup>47</sup> CJCE 18 July 2007, C-182/06, Lakebrink, [www.curia.eu](http://www.curia.eu).

<sup>48</sup> §25.

<sup>49</sup> §34.

Before the judgment in the Lakebrink-case was pronounced (and even before the opinion of the Advocate-General on this case)<sup>50</sup> the Dutch Hoge Raad had asked for a preliminary ruling in a slightly different context.<sup>51</sup> Again it considered taxation in a source state (the Netherlands, X) of a non-resident<sup>52</sup> (resident of Belgium, y) earning all of his professional income in the source state. This person however asked to take into account the 'negative income' from his own Belgian dwelling for the calculation of his taxable income, calculated according to the *Dutch* tax legislation. The Hoge Raad explained that this is income determined on a fixed estimated value of the immovable property, from which only interests and additional costs of a mortgage can be deducted.<sup>53</sup> As it had already previously concluded<sup>54</sup>, the Hoge Raad consequently expressly mentioned that the deduction of these costs was linked to the immovable property income, for which only Belgium had taxing competence.

However, on additional questions of the Court of Justice, the Dutch government responded that, based on the double tax convention with Belgium, for Dutch residents positive foreign immovable income is taken into account to determine the tax base. It is only in a secondary step exempted. Negative foreign income is also deducted, but a claw-back provision is foreseen in case of positive income of the same property in subsequent taxable years. The exclusion for non-residents is consequently a different treatment based on residence. Given the fact that Renneberg earned almost all of his income in the Netherlands (X), in Belgium a deduction would not be possible, even though a certain doubt was expressed about the existence of a correction in the Belgian tax legislation. Therefore, the Court concluded that the Netherlands had to accept a deduction of the foreign negative income, calculated according to *Dutch* tax criteria. As the comparison was made with a Dutch resident owning an immovable property in Belgium, the Court could not distinguish between personal dwellings and additional immovable properties. Its ultimate conclusion has been critically received in legal doctrine.<sup>55</sup>

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<sup>50</sup> The request had been formulated on 22 December 2006, whereas the conclusion in Lakebrink dates from 29 March 2007 and the judgment of the Court from 18 July 2007.

<sup>51</sup> CJCE 16 October 2008, C-527/06, R.H.H. Renneberg, [www.curia.eu](http://www.curia.eu).

<sup>52</sup> In the referring question for the Court the person was considered to be a non-resident. However, in reality this person was a resident of both the Netherlands and Belgium, but based on the double tax convention between both countries the Belgian qualification prevailed. Therefore more precisely this person could have been qualified as a 'limited resident taxpayer'. Cf. F.P.G. PÖTGENS en W.W. GEURSEN, "Renneberg: Is mortgage Interest Paid on an Owner-Occupied Dwelling in Belgium Deductible from Netherlands-Source Employment Income?", *E.T.* 2007, 499-500.

<sup>53</sup> At present this regulation figures in art. 3.120 Wet IB 2001.

<sup>54</sup> In a judgment of 2000 the Hoge Raad had to deal with the case of a resident of the Netherlands, working in the Netherlands, who moved to Belgium on 1 October 1995 in a newly build house. The discussion concerned the deduction of the difference between interest payments and the estimated value of the house for the three lasting months of 1995. The Dutch tax administration refused to take this 'negative income' into account when taxing the (at that time) non-resident. The Hoge Raad concluded that the difference between residents (who can deduct worldwide negative income) and non-residents was in line with the European legislation. Even though more than 90 % of the taxable income was earned in the Netherlands, the tax reduction based on the negative income from a foreign dwelling could, according to the Hoge Raad, not be considered to be an advantage based on the personal and family circumstances of the tax payer. Cf. H.R. 20 December 2000, nr. 35576, *BNB* 2001, 192, note I.J.J. BURGERS.

<sup>55</sup> Cf. E. KEMMEREN, "Renneberg Endangers the Double Tax Convention System or Can a Second Round Bring Recovery?", *EC Tax review* 2009, nr. 1, 4-15; G.T.K. MEUSEN, "Renneberg: ECJ Unjustifiably Expands Schumacker Doctrine to Losses from Financing of Personal Dwelling", *E.T.* 2009, 185-188.

From the preceding analysis it can be concluded that a distinction between income-related corrections and general corrections is not as such made in the jurisprudence of the Court when deciding which corrections a source state X should take into account based on the Schumacker-principles. However, when analyzing the tax treatment of particular income in a source state X, a non-resident y should, according to the court, receive all corrections linked to this income that are given to its own residents. Nonetheless, at the same time, it is not always clear to make this distinction in different tax correctives.

Returning to the particular case of Kieback, if he would have had during an entire tax year his German dwelling, while working in the Netherlands, he would have been entitled for the *Dutch* deduction for interest costs (mortgage payments). Given the fact that this deduction, calculated according to *German* tax law, could not be granted in Germany, the Court of Justice would consider Kieback being discriminated because his mortgage payments would nowhere have been taken into account. Although from a Dutch perspective these payments are closely linked with the German income, this would not change the outcome of the decision.

### All or nothing, but limited to tax legislation

In its reasoning the Court not only compares the treatment in a single source state X of a resident x and a non-resident y, but also departs from a conceptual principle that, in his tax treatment, a natural person at least has the right that one time his personal situation will be integrally taken into account to determine his applicable income taxes.<sup>56</sup> As tax legislation belongs to the autonomy of the Member states, a difference in such treatments in different Member states is acceptable. But a particular treatment in one state cannot negatively be influenced, because a person makes use of the freedom of movement. This holistic concept of non-discrimination explains why the Court demands a general treatment at the level of one single Member state as opposed to proportional treatments in each Member state where a tax payer would receive part of his income.

In most cases the personal situation can best be taken into account in the home state. In this case the mere earning of foreign income in another Member state cannot negatively influence this home state tax treatment. The Court clarified in different judgments that in such circumstances the moving tax payer would be discriminated vis-à-vis another resident only earning income in the home state.<sup>57</sup>

However, tax corrections in income taxation are generally based on an existing tax debt, making them useless for persons without tax debts. From the point of view of an individual compulsory social contributions and income taxes are sometimes combined to calculate the total of charges.<sup>58</sup> When looking from a supporting side however, social support<sup>59</sup> and tax

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<sup>56</sup> Cf. B. SANTIAGO, "Non-Discrimination Provisions at the Intersection of EC and International Tax Law", *E.T.* 2009, 258-259.

<sup>57</sup> Cf. CJCE 12 December 2002, C-385/00, F.W.L. De Groot; CJCE 12 December 2013, C-303/12, G. Imfeld and N. Garcet, [www.curia.eu](http://www.curia.eu).

<sup>58</sup> E.g. OECD (2014), Revenue Statistics 2014, OECD Publishing, [http://dx.doi.org/10.1787/rev\\_stats-2014-en-fr](http://dx.doi.org/10.1787/rev_stats-2014-en-fr).

<sup>59</sup> Nonetheless, the entitlement for social support often depends on the level of taxable income of a person, which is deduced from a tax declaration declaring taxable income in a previous tax year.

correctives are usually being dealt with separately. It is only for some rare particular incentives a tax corrective can be turned into a subsidy or social support.

Therefore, although a personal situation (e.g. children at charge) might have been taken into account for social remedies or support, as long as it has not influenced a person's taxable income, according to the Court of Justice it hasn't been taken into account. The concept of taking into account a personal situation is being analyzed from a general point of view, but nonetheless tax correctives are isolated from other possible corrections.

Because the non-resident y earns all of his taxable income in a source state X tax corrections cannot be applied in his home state Y. He is ultimately 'discriminated' in his tax treatment. This discrimination exists compared to residents of X working in X, as well as to residents of Y working in Y. For both categories the personal situation is taken into account when determining the income taxes due, while for y, making use of the free movement of workers, the personal situation is nowhere taken into account to determine his income taxes. A different treatment in both states is acceptable based on the Member states' autonomy, but conceptually the personal situation of y should have been taken into account once. This can best be resolved in the source state X as the non-resident earns most of his taxable income in this state.

The isolation of tax correctives also explains why, when determining whether (almost) all of a person's income is earned in a source state X, 'tax exempted income' (in a broad sense) is not being taken into account. According to the Court, a person receiving a 'non-taxable income' ('Stipendium') in his home state Y, is still entitled for a tax free minimum in the source state X, because otherwise his personal situation is not taken into account as far as the levying of income taxes is concerned.<sup>60</sup>

This leads to the conclusion that a separate analysis of the tax treatment has to be made, but all tax corrections (not directly linked to particular income) can be accumulated. A person can combine social measures of one legal system with tax correctives from another legal system and end up being favored. Divergences can also end up negatively, because of disparities<sup>61</sup>, which is neither solved.

The need for one general conceptual approach requires an indication of one Member State being the best placed to take into account a tax payer's personal situation. In general this is the residence state, unless this state is incapable of doing so. If a person y would reside in one state Y and earn all of his taxable income in two other different source states X and Z, the outcome is no longer clear. Again this person would be discriminated vis-à-vis residents of X, Y and Z working in their respective residence states. However, although Y cannot take

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<sup>60</sup> CJCE 1 July 2004, C-169/03, F.W. Wallentin, [www.curia.eu](http://www.curia.eu). In another case the Court decided that Germany (X) had to accept a tax deduction for household help of a couple living and working in Luxembourg and paying social contributions for this worker to the Luxembourg state under the Luxembourg regulation. Working for the European Communities most of their income was tax exempt, while in Germany this couple still had some taxable income. Cf. CJCE 13 November 2003, C-209/01, Schilling, [www.curia.eu](http://www.curia.eu).

<sup>61</sup> E.g. In Germany alimony payments are only tax deductible in case they are taxable for the receiver. A German resident x lost the deduction for these payments, when his wife moved to Austria, because the income is not taxed in Austria. Although the moving of his wife from Germany to Austria had a negative influence on the tax treatment of x, according to the Court this was not in violation of the free movement. Cf. CJCE 12 July 2005, C-403/03, Schempp, [www.curia.eu](http://www.curia.eu). (In its judgment the Court did not explicitly mention the concept of a 'disparity'.)

the personal situation into account, it is no longer clear which state should be responsible. The mere fact that the largest half of the taxable income would be earned in one source State is not an argument, as the tax corrections are not linked to the income. In line with previous judgments this would only indicate the relevant state if almost all of the taxable income is earned in one state.<sup>62</sup>

Another uncertainty rises if a person y earns a part of his taxable income in his residence state Y and a substantial part in another state X, while his taxable income in Y is lower than the maximum of tax corrections he would be entitled to according to the domestic tax legislation of Y. Again he will probably be discriminated against residents of X and Y earning the same taxable income completely in their respective residence states. An eventual benefit based on the lower tax rates because of the profit split of y cannot be considered to compensate this disadvantage.

These examples demonstrate that the conceptual all-or-nothing-approach in the verification of an existing discrimination is (only) from a particular scope. Other existing discrepancies still last. Additionally this approach obliges Member States to look at the tax treatment in another Member State which constitutes an infringement on their sovereignty.

Avery Jones suggested to solve this problem by replacing the exemption method with a credit method to avoid double taxation. The home state Y would always take all the income into account and consequently be the best placed to take into account the personal situation of an individual tax payer.<sup>63</sup>

A first remark to this solution is that particular exemption methods can obtain the same result. One could consider to take the worldwide income into account and subsequently give a credit for the domestic taxes calculated on the foreign income.<sup>64</sup> This would also allow the residence state to take into account the personal situation. More fundamentally however, obliging such particular relief method would largely limit a Member states' tax sovereignty to autonomously determine its own tax regime and contrast with the liberty being generally left to opt for a credit or exemption method.

It has also been suggested to replace this all-or-nothing-approach with a proportional approach. Each State would in this case offer personal allowances in proportion to the taxable income acquired on the territory.<sup>65</sup> This practice is sometimes agreed upon between two countries on a bilateral basis in double tax conventions.<sup>66</sup>

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<sup>62</sup> In a judgment of 22 May 2015 the Dutch Hoge Raad referred a new case to the Court of Justice. (Case C-283/15). It concerned a Spanish resident earning income from services executed all over the world, but from which 60 % would be taxable in the Netherlands and 40 % would be taxable in Switzerland. Cf. H.R. 22 May 2015, nr. 13/03468, [www.rechtspraak.nl](http://www.rechtspraak.nl). The Dutch Advocate-General advised to refer the case to the Court of Justice, but also expressed a favor of granting the personal allowances in each source state, but in proportion to the number of source states concerned.

<sup>63</sup> J.F. AVERY JONES, "A Comment on "Progressive Taxation of Non-Residents and Intra-EC Allocation of Personal Tax Allowances"", *E.T.* 2000, 375.

<sup>64</sup> E.g. the exemption method as applied in the Netherlands.

<sup>65</sup> P.J. WATTEL, "Progressive Taxation of Non-Residents and Intra-EC Allocation of Personal Tax Allowances: Why Schumacker, Asscher, Gilly and Gschwind Do Not Suffice", *E.T.* 2000, 210-223. Compare with the proposal of Schön to align general business expenses of a company over all Member States where it has earned income. Cf. J. SCHON, "Neutrality and Territoriality – Competing or Converging Concepts in European Tax Law?", *B.I.T.* 2015, 286.

<sup>66</sup> E.g. the Belgian conventions with France, Netherlands and Luxembourg (only for Luxembourg residents earning Belgian income).



However, as already mentioned, as the level of comparing only focuses on the tax regime, this would still generate discrimination possibilities, in case of corrections based on social measures.

Additionally, it is not clear whether all kinds of existing tax corrections are able to be given for a part of the taxable income. E.g. the advantage of splitting income between spouses depends on a comparison of the taxable income of both partners. How does this comparison has to be made in a source state where only one of both partners earns (a part of his) taxable income? What to do with other correctives that depend on the total of taxable income ?<sup>67</sup>

Finally, supposing that a formula for each tax correction could be found, given the difficulties that arise already between two countries, generalizing such approach on a multilateral level would cause a nightmare for tax administrations. Source states where only a small part of someone's taxable income has been realized, would face an intolerable overwhelming administrative burden.

It can be concluded that the European approach also looks from an abstract point of view, taking into account the (general, but only) tax situation of a particular tax payer, ensuring that he has at least in one state all existing corrections be applied to him. In an abstract comparison one has to look for the state which is best placed to offer its domestic tax corrections. A proportional application based on the amount of taxable income is not applied.

If Kieback (y) would have worked an entire tax year in the Netherlands (X), while residing in Germany (Y), he would be discriminated vis-à-vis Dutch workers having the same activity in the Netherlands, as well as vis-à-vis German workers earning taxable income from a similar activity in Germany. Would he move his residence from Germany to e.g. Belgium and stay working almost exclusively in the Netherlands he would in addition be discriminated vis-à-vis Belgian workers working in Belgium. The Netherlands could in this context still be considered to be the best placed Member State to solve this discrimination. Probably the Dutch tax legislator would still have to offer Kieback all of the personal allowances given to Dutch residents in the same situation as Kieback.

### Possible influence of a timing concept ?

The last question concerns the effect of splitting the tax year, because of moving to another residence state, which is combined with the ending up of the activity in the source state. In its referring judgment the Dutch Hoge Raad made an explicit reference to the time period. Although in practice this complication was also present in other earlier cases, it only appeared implicitly.

As already mentioned, the Schumacker-case concerned a person working from 15 May 1988 until 31 December 1989, starting a procedure (already) on 6 March 1989. In this case

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<sup>67</sup> Compare with the Dutch application of a pro rata in the tax treaty with Belgium. Although the treaty demands a pro rata acceptance, the Secretary of State accepted a full taking into account of so-called 'heffingskortingen', while applying the pro rata only for 'heffingvrij vermogen' and 'persoonsgebonden aftrekposten'. Cf. Decree of 20 April 2010, DGB2010/568M, Dutch Gazette 2010, 6364, [www.wetten.overheid.nl](http://www.wetten.overheid.nl).



however, the Court did not seem to take this aspect into account as the questions were formulated in a rather general way.

However, even before the Schumacker-case, to a certain extent the Biehl case can be mentioned.<sup>68</sup> In the year 1983 Biehl was living and working in Luxembourg until 31 October and then moved to Germany and started working there. A withholding tax had been deducted on his salary<sup>69</sup>, which exceeded his income taxes due. However, the Luxembourg tax administration refused to pay back the excessive taxes, because this procedure would only exist for persons being resident of Luxembourg the entire tax year. The Court of Justice did not accept this distinction. The general assumption that a progressive tax rate would favor moving persons could not justify the existing discrimination. The case however differs from the Kieback-case as it focuses on a home state and imputation possibilities of withholding taxes. It nonetheless illustrates that a home state cannot make a general<sup>70</sup> difference in taxation between persons that are only resident for a part of a tax year and persons residing in the state the whole tax year.

Another interesting case is Wallentin.<sup>71</sup> This case concerned a German student and resident, who stayed in Sweden from 1 July till 20 August 1996 for a paid traineeship with the Swedish Church (from 3 till 25 July).

The Swedish tax legislation distinguished between people residing in Sweden for less than 6 months, people residing in Sweden for at least 6 months but lesser than a year, and people residing in Sweden a full tax year. The last category benefitted from a tax free minimum income, the second category received this partially, in proportion to the length in time of their stay in Sweden, while the first category was excluded from this tax benefit. As Wallentin only stayed in Sweden for two months an application of the tax free minimum was refused to him.

In Germany Wallentin received a tax exempt so-called 'stipendium' from the German government, as well as a monthly allowance of his parents. Both payments were not considered as taxable income. Therefore Wallentin could not make use of any tax corrective in Germany considering his personal situation and claimed the entire Swedish tax free minimum for Swedish residents.<sup>72</sup>

Although Wallentin *resided* for two months in Sweden, the referring Court asked the Court of Justice whether the distinction of the Swedish system between non-residents (being taxed at a lower tax rate, but without tax correctives for a personal situation) and residents (taxed at a higher progressive tax rate, but with additional personal allowances) was in line with the free movement of workers. It is also remarkable that the precise time lapse was hardly taken into consideration, despite of the existing distinction in the Swedish legislation.<sup>73</sup>

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<sup>68</sup> CJCE 8 May 1990, C-175/88, Biehl, [www.curia.eu](http://www.curia.eu).

<sup>69</sup> Probably the withholding tax was based on the assumption Biehl would work the whole year in Luxembourg.

<sup>70</sup> The Court did not accept this regulation because it could be a discrimination in case a person would not earn taxable income in the other state. In its judgment the Court also took into account the existence of an administrative procedure taking away discriminative effects. However, as this procedure was not binding and could not guarantee to take away all discriminative effects, it could not justify the distinction.

<sup>71</sup> CJCE 1 July 2004, C-169/03, Wallentin, [www.curia.eu](http://www.curia.eu).

<sup>72</sup> This would mean an accumulation of a social corrective (nontaxable income in Germany) and a tax corrective (tax free minimum in Sweden).

<sup>73</sup> The Swedish tax administration compared Wallentin with other temporarily residents and stated that a maximum *pro rata* of two months would have to be accorded, while Wallentin claimed an entire allowance. The Court of Justice decided that "*at the material time*" Wallentin could not enjoy comparable benefits in his

The Court considered the Swedish tax system an infringement of the free movement of workers in the general terms linked to the question.<sup>74</sup>

In these judgments it seems that the Court does not accept a time difference as a general justification for a negative tax effect.<sup>75</sup> The comparison between home and source state further has to be made at an abstract level comparing which state is best placed to grant tax correctives linked with the personal situation of a tax payer. A short stay in a state is in itself no argument for an exclusion of benefits.

In general, one could implicitly accept that some tax correctives are linked with a tax year.<sup>76</sup> However, given the rather general description, this does not necessarily have to be the case. E.g. negative income from a personal dwelling could be linked to the condition of actually living in this immovable property, which might in some domestic tax regimes be determined on a monthly, instead of a yearly basis. Given the wide range of possible tax correctives, as well as the tax sovereignty for each Member state to determine its correctives, it seems appropriate giving States the authority to decide how their correctives are to be attributed. If for their own residents it is possible to grant a tax corrective for a proportional time period, it must be considered also accessible for non-residents, if they are entitled to certain tax benefits based on the Schumacker-principles as being explained.

From an abstract point of view, a resident Y earning during a certain period of time almost all of his taxable income in X and then moving to Z and earning all of his income in Z would be discriminated compared to residents of X and Y, if his personal situation was not entirely taken into account in either of the three states, while residents of X and Y working in their respective home state and moving to Z would (proportionally) be entitled for tax benefits in both home states (X and Z or Y and Z).

As in the previous cases the question rises which state would be best placed to take into consideration the personal situation.

It might be possible that state Z takes into account the situation existing at the end of the tax year to determine the tax benefits for an entire tax year. However, most states will (as state Z) apply a proportional approach taking into account the period the tax payer was a resident. This differs from a proportional approach based on the percentage of income earned and is much more easy to determine. If the tax payer can demonstrate that his personal situation (for the period before becoming a resident of Z) has not been taken into account in Z, he is discriminated versus residents of X and Y working in their home state. If additionally state X applies a proportional approach for its own residents, there seems to be no justification for not granting the same benefit to non-residents Y earning most of their taxable income during a certain period in X.

The tax treatment in X is in this situation determined by the tax treatment in other states, but this is an overall consequence of the Schumacker-principles. The proportional approach would probably (a bit) complicate the calculation, but the possibility to grant such

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home state, without further explaining which period it meant. (Cf. in particular §18). Only Advocate-General Léger refers in his conclusion explicitly to the entire tax year 1996. (Cf. §31 Concl.)

<sup>74</sup> After this judgement Sweden introduced an option for the non-resident to be taxed as a resident. This system was recently approved by the Court of Justice. Cf. CJCE 19 November 2015, C-632/13, Hirvonen, [www.curia.eu](http://www.curia.eu).

<sup>75</sup> Although the referring questions were rather general, nonetheless the Court itself did not adjust this either.

<sup>76</sup> Some Belgian personal tax correctives (e.g. children at charge) are based on the situation existing when the tax year ends. This situation is taken into consideration for the entire tax year.

proportional tax corrective was the autonomous sovereign choice of a State. If State X decides it can determine the entitlement for personal tax correctives based on the ability to pay taxes on a partial basis, this option must also be given to non-residents y.

The conclusion of the Court of Justice on this particular point therefore is hard to accept. As already mentioned the situation would be different in case of a non-resident y working in X during a certain period of time and then working in Z, but keeping its residence in Y. In this last case, there would be no particularly defined source state, while the personal situation giving rise to the tax correction is not interrupted. However, in the case of Kieback, source state X (the Netherlands) provides for the possibility of a proportional calculation and the situation giving rise to the tax corrective is also clearly linked to the period Kieback was working in X. If it is accepted that a source state X has to take into account mortgage payments for an immovable property situated in another state and that a discriminative treatment can be judged upon from the abstract point of view of an individual tax payer, the treatment of Kieback in the Netherlands should have been the same as the treatment of a resident of the Netherlands moving to the US.

## ***Conclusion***

This article criticizes the judgment of the Court of Justice in the Kieback-case. This case concerns a person, moving in a particular civil year from Germany to the United States. When living in Germany he works (and receives most of his taxable income) in the Netherlands, while in Germany he pays mortgage payments for a personal dwelling. When he moves to the United States, he also starts working there. As he moves after three months, he earns most of his income in the particular civil year in the United States. However, as during his residency in Germany, he earns most of his income in the Netherlands, based on the Schumacker-principles, he claims the deduction of the German payments from his Dutch taxable income, which the Dutch tax administration refuses. The domestic courts, as well as the European Advocate-General concluded that Kieback was entitled for this deduction. The Court of Justice nonetheless answers that the 'Schumacker-criterium' (whether a non-resident has earned almost all of his taxable income in a source state) has to be verified on a yearly basis, instead of a proportional application.

The article first refers to the application of the Schumacker-principle on a deduction for mortgage payments linked to a foreign immovable property. The author concludes that, although a particular state can make a distinction between income-related tax allowances and tax corrections for a personal situation, this distinction is not always necessarily clear, which is demonstrated with the example of a deduction for mortgage payments. The Court does not make this particular distinction causing a source state having to take into account tax deductions linked to the foreign income in another state.

In a second step the author demonstrates that the analysis of the court in case of free movement not only looks at the particular regulations from the point of view of a particular Member state, but also verifies from the point of view of an individual tax payer whether or not he is being discriminated. Finally, taking into account both foregoing premises, the author does not support the final conclusion of the Court that the so-called Schumacker-criterium only has to be verified on a yearly basis.