OPINION OF ADVOCATE GENERAL LÉGER

delivered on 31 May 1995 *

1. The list of judgments of the Court of Justice examining the compatibility of domestic rules on direct taxation with the principle of freedom of movement for persons is already long. [1] The tax chamber of the Gerechtshof te 's-Hertogenbosch now asks the Court to interpret Article 52 of the EC Treaty as it applies to the Netherlands pension-reserve system ('oudedagsreserve').

2. Article 1 of the Netherlands Law on Income Tax of 16 December 1964 [2] defines 'national taxpayers' as natural persons resident in the Netherlands as opposed to 'foreign taxpayers', natural persons who are not resident in the Netherlands but who do receive income there.

3. By the Law of 16 November 1972, [3] supplementing the 1964 Law, the Netherlands legislature established a voluntary pension-reserve tax scheme for self-employed persons [4] permitting them to 'reserve' a proportion of the profits of their business to form a pension reserve — without precluding membership of a collective pension scheme. The pension-reserve has the advantage that the amounts set aside remain in the business. It is distinguished by very favourable tax treatment.

4. Under the third paragraph of Article 3 of the 1964 Law, sums 'reserved' each year are deductible from taxable profits. [5] The pension reserve must be liquidated when the taxpayer reaches the age of 65. [6] The accumulated reserve is then treated as 'income' and taxed either once on the capital or on the payments made periodically (where the capital is converted into periodic payments). The 'reserved' sums are thus subject to *deferred taxation*.

5. Pursuant to Articles 48 and 49 of the 1964 Law, foreign taxpayers are taxed solely on their 'taxable national income' comprising their total income in the Netherlands during a calendar year reduced by losses. Article 48(3) provides that certain deductions, which

* Original language: French.

1 — See point 1 of my Opinion in Case C-279/93 *Finanzamt Köln-Altstadt* v *Schumacker* [1995] ECR I-225.

2 — Nederlandse wet op de inkomstenbelasting 1964, *Staatsblad* 519 (hereinafter 'the 1964 Law').

3 — *Staatsblad* 612.

4 — Article 44*d*(1).

5 — Article 3(3) provides: 'Income is gross income: (a) reduced by amounts added and increased by amounts withdrawn from the pension-reserve ...'

6 — Article 44*f*(1)(e).

do not include the pension reserve, may be made from that income.

6. Consequently it can be seen from Articles 3(3) and 48(3) of the 1964 Law that national taxpayers have an advantage (the possibility of making deductible old-age insurance provision) which is denied to foreigners.

7. Foreigners are denied a number of benefits and in particular the possibility of deducting personal commitments and extraordinary charges [7] because it is assumed that those items will be taken into account by the tax authorities of the State of residence. A ministerial circular provides however for a correction where at least 90% of the non-resident taxpayer's world-wide income is subject to income tax in the Netherlands: [8] deductions are then permitted. That circular does not however cover pension reserves.

8. That is the legislative background to the questions referred by the national court.

9. A Belgian national resident in Belgium, Mr Wielockx is a partner in a physiotherapy practice in Venlo, the Netherlands. He has no other job and receives no other income, in particular in Belgium.

10. By virtue of the double-taxation convention between Belgium and the Netherlands, [9] Mr Wielockx is liable to pay tax in the Netherlands. [10]

11. He disputes his tax assessment for 1987.

12. He sought to deduct from his taxable income for that year (HFL 73 912 reduced to HFL 65 643 by the tax authorities) the sum of HFL 5 145 by way of the pension reserve; the tax authorities refused. Mr Wielockx

7 — Article 48(3) of the 1964 Law.

8 — Ministerial circular ('resolutie') No DB 91/481.

9 — Article 7(1) of the Convention of 19 October 1970, *Tractatenblad*, 1970, No 192.

10 — Although the question whether Article 7 or Article 14 applies is a matter of dispute between the *juge a quo* and the Commission (see paragraph 18 of the latter's observations).

brought an action before the tax chamber of the Gerechtshof te 's-Hertogenbosch which has referred three questions to the Court for a preliminary ruling. The questions may be summarized as follows:

(1) Does Article 52 of the Treaty preclude a Member State from refusing the right to set up a deductible pension reserve to non-resident taxpayers?

(2) If there is discrimination, is it justified by the fact that the deductibility of amounts added to the pension reserve could not, in so far as concerns non-resident taxpayers, be counterbalanced by the fact that amounts withdrawn are taxable?

(3) Is it relevant whether the foreign taxpayer received all or almost all his income in the State of employment?

13. I will consider the first and third questions together.

The first and third questions

14. It is self-evident that Article 52 of the Treaty applies: Mr Wielockx has used his freedom of movement within the Community to establish himself as self-employed in the Netherlands.

15. It is equally clear that, although direct taxation falls within the powers of the Member States, '... the powers retained by the Member States must nevertheless be exercised consistently with Community law ...'. [11] The Court has concluded from that that Article 48 of the Treaty was '... capable of limiting the right of a Member State to lay down conditions concerning the liability to taxation of a national of another Member State and the manner in which tax is to be levied on the income received by him within its territory, since that article 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 State in the exercise of his right of freedom of movement less favourably than one of its own nationals in the same situation.' [12]

11 — Paragraph 21 of *Schumacker*, cited above, note 1.
12 — Ibidem, paragraph 24.

16. For the same reason, I draw the same conclusion in relation to Article 52 of the Treaty which the Court has moreover already reached in the area of direct taxation in *Commission* v *France* (the 'avoir fiscal' case), [13] *Commerzbank*, [14] and *Halliburton Services*. [15]

17. Until now, the Court has always considered that Article 52 of the Treaty, applied to the area of taxation, requires — in the same way as Article 48 — evidence of overt or covert discrimination. It may however by noted in passing that measures applicable without distinction may have an equally restrictive effect on freedom of movement for persons or freedom of establishment as discrimination. [16]

18. Is it possible to find covert discrimination based on nationality in the criterion of residence?

19. The Court has consistently held [17] that a distinction based on residence, even though applicable without distinction to nationals and non-nationals, may mask a distinction based on nationality. Denying non-residents '... certain benefits which are, conversely, granted to persons residing within national territory, [is] liable to operate mainly to the detriment of nationals of other Member States. Non-residents are in the majority of cases foreigners.' [18]

20. Is there however discrimination in a situation such as that before the Court, namely the application of different rules to comparable situations?

21. The criterion of residence as it is used by international tax law is not in itself contrary to Community law. I refer on this point to my Opinion in *Schumacker* [19] and to the judgment in that case, in which the Court explained the logic behind the distinction between residents and non-residents:

'In relation to direct taxes, the situations of residents and of non-residents are not, as a rule, comparable.

13 — Case 270/83 [1986] ECR 273.

14 — Case C-330/91 [1993] ECR I-4017.

15 — Case C-1/93 [1994] ECR I-1137.

16 — P. Farmer and R. Lyal, *EC Tax Law*, Clarendon Press — Oxford, 1994, p. 331.

17 — Case C-175/88 *Biehl* [1990] ECR I-1779, paragraph 14; Case C-204/90 *Bachmann* [1992] ECR I-249; *Commerzbank*, cited above, paragraph 14 and *Schumacker*, cited above, note 1, paragraph 26.

18 — *Schumacker*, cited above in note 1, paragraph 28.

19 — Cited in note 1 above, points 35 to 38. See also points 37 to 39 of the Opinion of Advocate General Darmon in *Commerzbank*, cited above.

Income received in the territory of a Member State by a non-resident is in most cases only a part of his total income, which is concentrated at his place of residence. Moreover, a non-resident's personal ability to pay tax, determined by reference to his aggregate income and his personal and family circumstances, is more easy to assess at the place where his personal and financial interests are centred. In general, that is the place where he has his usual abode. Accordingly, international tax law, and in particular the Model Double Taxation Treaty of the Organization for Economic Cooperation and Development (OECD), recognizes that in principle the overall taxation of taxpayers, taking account of their personal and family circumstances, is a matter for the State of residence.

The situation of a resident is different in so far as the major part of his income is normally concentrated in the State of residence. Moreover, that State generally has available all the information needed to assess the taxpayer's overall ability to pay, taking account of his personal and family circumstances.' [20]

22. It follows that, since residents and non-residents are not objectively in the same situation, the difference in treatment between those two categories of taxpayers cannot be regarded as discrimination within the meaning of the Treaty.

23. On the other hand, a non-resident worker who receives income only in the State of employment is objectively in the same fiscal situation as a resident of that State with the same job. He has the same taxable income: his taxable amount is the same. However, his personal and family situation will be taken into account neither by the tax authorities of that State (because he is not resident there) nor by the tax authorities of the State of residence (because he has no income there and is therefore not liable to pay tax there). The Court has found discrimination in that situation. [21]

24. In the Netherlands, the rules applicable to the taxation of residents are, for calculating Netherlands income, generally applicable by analogy to non-residents. [22] However, non-residents do not benefit from the same scope for deduction as residents. [23]

25. In the situation in question, a resident in a Member State may deduct from his taxable income the proportion which he pays into his pension-reserve account. A non-resident who receives all his income in that State — and who is hence in the same fiscal situation as the resident — is not entitled to form such a reserve. [24] Although a self-employed resi-

20 — Paragraphs 31 to 33.

21 — *Schumacker*, cited above, paragraph 38.

22 — Article 48(4) of the 1964 Law.

23 — Ibidem, Article 48(3).

24 — Resolution No DB 91/481 — which it will be recalled permits a non-resident receiving at least 90% of his income in the State of employment to be treated like a resident — does not apply to the pension reserve.

dent may form a pension reserve and thus benefit from a *fiscal advantage*, that possibility is denied to a self-employed non-resident. If the latter contemplates making provision for his retirement, he does not have as wide a choice as a resident since he does not have access to the pension reserve.

26. I regard that as discrimination which however affects only a self-employed non-resident who receives all or almost all his income in the State of employment. It is only in those circumstances that he is in a comparable fiscal situation to a self-employed resident. He is taxed by the State of employment alone, as is a resident of that State. On the other hand, it may be the case that, if the non-resident has income in his State of residence and is liable to pay tax there, he will have a number of advantages, in particular the possibility of deducting certain sums set aside as savings. In any event, that taxpayer is not in the same fiscal situation as the national.

27. It follows that whether the taxpayer receives all his income in the State of employment is decisive for answering the third question. It is only in the event that he receives all or almost all his income in the State of employment that he must be considered to be the victim of discrimination.

28. I conclude that Article 52 of the Treaty precludes legislation of a Member State, such as the Netherlands pension-reserve tax rule, which allows a tax deduction reducing the taxable income of self-employed residents but denies it to self-employed non-residents who receive all or almost all their income in that State.

29. Now that discrimination has been established, it must be considered whether it is justified.

The second question

30. The question of justification and the possible applicability of the principle of fiscal cohesion as laid down by the Court in *Bachmann* [25] and *Commission* v *Belgium* [26] is extremely delicate.

31. It is clear from those two judgments that the Court accepts that, in the area of tax, discriminatory national rules may be justified for imperative public-interest requirements

25 — Cited in note 17 above.
26 — Case C-300/90 [1992] ECR I-305.

other than those set out in the Treaty, and in particular in the name of the cohesion of the tax system. [27]

32. The *Bachmann* case arose in the following circumstances: Mr Bachmann, a German national employed in Belgium after working in Germany, challenged the refusal by the Brussels Director of Direct Taxation to allow the deduction from his total earned income in Belgium of contributions paid in Germany under sickness-and invalidity-insurance and life-assurance policies entered into in Germany before he came to Belgium.

33. The Director of Taxation relied on Article 54 of the Belgian Income Tax Code which provided that sickness-and invalidity-insurance or pension and life-assurance contributions are deductible from earned income only if paid in Belgium.

34. In reply to the questions referred for a preliminary ruling by the Belgian Court of Cassation, the Court of Justice found in that provision discrimination against migrant non-resident workers incompatible with Article 48 of the Treaty. [28] The Court considered that that discrimination was justified given the *correlation* which existed in the Belgian tax system between the deductibility of the contributions and the taxation, when the pension and life-assurance policies matured, of the capital sum insured or the annuity paid by the insurance company [29] (conversely, parties to such contracts of insurance who have not had the right to deduct are not liable to pay tax on the capital sums, pensions or annuities paid under those contracts [30]). 'The cohesion of such a tax system ... therefore presupposes that, in the event of a State being obliged to allow the deduction of life assurance contributions paid in another Member State, it should be able to tax sums payable by insurers.' [31]

35. Consequently, the Belgian tax authorities were entitled to refuse to allow deduction of the premiums paid to companies not established in Belgium since they could not be certain of taxing the capital sum or annuities paid out in consideration. *Those payments could be taxed neither at source (the insurance company liable to make the payments is established in another Member State) nor in the hands of the recipient (resident in another Member State).*

27 — See my Opinion in *Schumacker*, cited above, points 47 and 48. See also D. Fosselard, 'L'obstacle fiscal à la réalisation du marché intérieur', *Cahiers de droit européen*, 1993, p. 472, 482; P. Farmer and R. Lyal, op. cit.: 'The judgment in *Bachmann* indicates that covertly discriminatory tax rules can sometimes be justified by imperative requirements', p. 330.

28 — *Bachmann*, cited above, paragraph 9, and *Commission* v *Belgium*, cited above, paragraph 7.

29 — *Bachmann*, paragraphs 21 to 23, and *Commission* v *Belgium*, paragraphs 14 to 16.

30 — Article 32a of the Belgian Income Tax Code.

31 — *Bachmann*, paragraph 23.

36. The Court, having applied a test of proportionality, was satisfied that that cohesion could not be protected by other measures with a less restrictive effect on freedom of movement for persons, such as an undertaking by an insurer to pay the tax or provision in a bilateral convention for the deduction of contributions paid in a State other than that allowing the deduction. [32]

37. Several commentators on *Bachmann* have argued — to my mind convincingly — that national rules which better observed the principle of freedom of movement for persons and freedom of establishment could have enabled Belgium to arrive at the same result. [33] I do not propose to enter into that debate.

38. *Bachmann* is interesting because of the step taken by the Court: Member States — which have exclusive competence in the current state of Community law to formulate their tax system [34] and decide, for example, to promote saving by tax incentives or to align the tax treatment of self-employed persons' pensions with that of employees' pensions — may adopt discriminatory measures if those measures are justified by public-interest reasons and essential for attaining their objective. Applying a proportionality test — which must in my view be strict where a discriminatory measure is at issue — must enable it to be ascertained whether the measure was necessary for the attainment of the objective pursued.

39. Setting up a coherent tax system is a legitimate objective for the purposes of Community law [35] in the sense that it may in certain specific cases justify restrictions on freedom of movement for persons and even discriminatory measures.

40. If the examples of discrimination found in *Commission* v *France* (the 'avoir fiscal' case), cited above, *Biehl* [36] or *Commerzbank*, cited above, were not in any way essential to protect the cohesion of the tax system at issue, it is in contrast clear from *Bachmann* that, in order to implement a fiscal policy encouraging individuals to make provision by saving, a Member State is entitled to require that the deductibility of life-assurance contributions paid in its territory

32 — See *Bachmann*, paragraphs 24 to 27; *Commission* v *Belgium*, paragraphs 17 to 20, and *Schumacker*, paragraph 21.

33 — Farmer and Lyal, op. cit., p. 333; W.-H. Roth, 30 *Common Market Law Review* (1993), 387-395; L. Hinnekens and D. Schelpe (1992) *EC Tax Review*, p. 58.

34 — See *Bachmann*, paragraph 23, and *Commission* v *Belgium*, paragraph 16.

35 — '... the *Bachmann* cases are no more than a recognition by the Court that Member States, in devising a coherent national tax regime, pursue a goal which is justified under Community law' (J. Wouters, 'The Case-Law of the European Court of Justice on Direct Taxes: Variations upon a Theme', 1 *Maastricht Journal of European and Comparative Law* (1994) 179, 203).

36 — Cited in note 17 above.

is counterbalanced by the taxation in that State of the capital or annuities paid in consideration. It may deny non-residents that right of deduction if it cannot tax the annuities which they receive abroad.

41. Let us apply that test of proportionality to the situation at issue.

42. Is the pension-reserve scheme comparable to the life-assurance and old-age pension insurance contracts referred to in *Bachmann*? Can the reasoning followed in that case be extrapolated to this case?

43. The pension reserve is designed to enable self-employed persons to have the benefit of a retirement scheme comparable to that available to employees.

44. The pension reserve is an alternative to other forms of pension. Thus the maximum annual contribution to a pension reserve is reduced by the amount of any premium paid pursuant to compulsory membership of an occupational pension scheme. [37]

45. The drafting history of the 1972 law which established the pension reserve shows that that reserve has specific features which are extremely significant. Unlike contributions to a pension fund, the proportion of profits allocated to the pension reserve remains part of the assets of the undertaking and may be used by it: '... materieel houdt dit in dat de belastingheffing over een deel van de winst wordt uitgesteld, opdat:

— vermogen voor de oudedag kan worden gespaard, en

— het aldus gespaarde vermogen kan worden aangewend in de onderneming'. [38]

46. This provides an additional reason for the Member State to require a correlation between the deductibility of the contributions and the taxation of the pensions. The pension reserve confers on the undertaking an exceptional advantage which would not be provided by a life-assurance or life-annuity scheme. It enables the self-employed

37 — See paragraph 13 of the Commission's observations.

38 — See *Memorie van Toelichting*, No 3, Zitting 1971-1972, 11818.

person to set up a retirement fund for himself out of the profits of the business without however reducing the business assets, while providing that the sums set aside are deductible from taxable income. It must be possible to counterbalance that advantage by a correlative taxation of the capital or periodic payments made during the businessman's retirement.

47. Since *Bachmann* it has been clear that, in the name of the principle of the cohesion of the tax system, a Member State is free to base the tax regime applying to a particular type of pension on a principle of correlation between the deductibility of the contributions (granted for social reasons or to promote the financing of undertakings) and the taxation of the pensions (necessary for budgetary reasons). [39]

48. Does that cohesion justify discrimination against non-residents?

49. In my view, discrimination cannot be justified by the cohesion of the tax system for the following reason: it is not certain that the State concerned bases the cohesion of its tax system on the principle of the correlation between deductibility of contributions and taxation of retirement pensions (and between deductibility of the 'reserved' sums and taxation of the periodic payments made from the pension reserve).

50. This is because:

51. A State may base the cohesion of its tax system on a principle of correlation between deductibility of contributions and taxation of pensions. *It may also reject that principle.*

52. Article 18 of the OECD draft convention [40] provides: 'Subject to the provisions of paragraph 2 of Article 19 [concerning civil servants' pensions], pensions and other similar remuneration paid to a resident of a Contracting State in consideration of past employment shall be taxable only in that State.'

53. In this way in the Community the Member States have agreed in a very general fashion, in accordance with the OECD draft convention, to make the payment of contributions deductible and to tax the periodic payments made in consideration in the State of residence. For example, the insured under

39 — See J. Wouters, op. cit., p. 203.

40 — Model Double-Taxation Convention on Income and on Capital, Report of the Committee on Fiscal Affairs of the OECD, 1977.

an old-age insurance policy who pays contributions in the Netherlands and spends his retirement in Belgium will be taxed on his retirement pension in the latter State and will not have to pay tax in the Netherlands. [41]

54. The effect of the double-taxation conventions which are an integral part of national tax law and override domestic tax rules is that the cohesion applies *at another level*: the State taxes all pensions received by residents in its territory, whatever the State in which the contributions were paid. Conversely, it waives the right to tax pensions received abroad even if they derive from and are made in consideration of contributions paid in its territory which it treated as deductible. [42]

55. That is the import of the double-taxation conventions applicable to the proceedings pending before the national court. The result is a pension system set up for self-employed persons which does not require a rigorous correlation between deductibility of contributions and taxation of pensions in order to secure its cohesion.

56. The Court may however consider, as it did in *Bachmann*, [43] that bilateral conventions must be interpreted with caution and that it cannot be inferred from the convention in question that the State of employment has renounced the principle of correlation between deduction of the 'reserved' sums and taxation of the periodic payments made from the pension reserve.

57. I accordingly propose to make the following observations in the alternative:

58. I do not consider that the cohesion relied on by the Netherlands Government justifies discrimination against non-residents.

59. The situation before the Court may be distinguished on a key point from that in *Bachmann*:

60. As I have stated, [44] in the latter case the Belgian State could not tax the annuities or benefits paid either at source or in the hands of the recipient.

41 — Pursuant to Article 18 of the Double-Taxation Convention of 19 October 1970 between the Kingdom of Belgium and the Kingdom of the Netherlands on Income and Capital and Certain Other Fiscal Matters (*Moniteur belge* of 25 September 1971, Code Larcier, Volume IV, 1990, p. 704) which reproduces word for word Article 18 of the OECD draft convention. See also Article 22 of the Belgium-Netherlands convention: 'Income of a resident of one of the States to which the preceding articles of this convention do not apply shall be taxable only in that State.'

42 — On this point, see L. Hinnekens and D. Schelpe, op. cit., p. 62.

43 — Paragraph 26.

44 — See point 35 above.

61. Here the situation is entirely different: until liquidated, the pension reserve never leaves the assets of the undertaking and is subsequently liquidated *by the undertaking* either as capital or as periodic payments in respect of which the debtor is the undertaking itself and the creditor is the beneficiary of the pension reserve.

62. Clearly tax cannot be levied on the latter: he is non-resident.

63. It may however be levied at source on the undertaking which is — by definition — established in the Netherlands.

64. In *Bachmann*, the Court ruled that an undertaking by an insurer *established in another Member State* to pay such tax could not constitute an adequate safeguard. [45]

65. Here the debtor in relation to the pensions — the undertaking — remains *established in the Netherlands*: an undertaking by it to pay the tax on the pensions would constitute an adequate safeguard.

66. It could be argued that the principal obstacle to such a system is the double-taxation convention between Belgium and the Netherlands which provides for taxation in the State of residence. It follows that the State of employment is prohibited from taxing pensions paid to non-residents.

67. The Court has already held in *Commission* v *France* (the 'avoir fiscal' case), cited above, that a bilateral convention cannot justify or be the basis of an infringement of Community law:

'... the rights conferred by Article 52 of the Treaty are *unconditional* and a Member State cannot make respect for them subject to the contents of an agreement concluded with another Member State.' [46]

68. Consequently the discriminatory legislation at issue does not stand up to the test of proportionality laid down by *Bachmann*.

45 — Paragraph 24.

46 — Paragraph 26, emphasis added.

69. I therefore propose that the Court should rule as follows:

Article 52 of the Treaty precludes legislation of a Member State, such as the Netherlands pension-reserve tax rule, which allows a tax deduction reducing the taxable income of self-employed residents but denies it to self-employed non-residents who receive all or almost all their income in the State of employment.