JUDGMENT OF THE COURT (Third Chamber)

19 January 2006 *

In Case C-265/04,

REFERENCE for a preliminary ruling under Article 234 EC from the Kammarrätten i Sundsvall (Sweden), made by decision of 17 June 2004, received at the Court on 24 June 2004, in the proceedings

Margaretha Bouanich

v

Skatteverket,

THE COURT (Third Chamber),

composed of A. Rosas, President of the Chamber, J. Malenovský, S. von Bahr, A. Borg Barthet and U. Lõhmus (Rapporteur), Judges,

* Language of the case: Swedish.

Advocate General: J. Kokott,
Registrar: R. Grass,

having regard to the written procedure,

after considering the observations submitted on behalf of:

— Ms Bouanich, by J. Grönlund, skattejurist,

— the Swedish Government, by A. Kruse, acting as Agent,

— the Commission of the European Communities, by R. Lyal and L. Ström van Lier, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 14 July 2005,

gives the following

Judgment

1 This reference for a preliminary ruling concerns the interpretation of Articles 43 EC, 48 EC, 56 EC and 58 EC.

2 The reference was made in proceedings between Ms Bouanich, a French national and shareholder in a Swedish public limited company, Förvaltnings AB Ratos ('Ratos'), and the Skatteverket (Swedish Local Tax Board) concerning the latter's refusal to refund to Ms Bouanich the whole amount of the tax charged on the repurchase of her shares by that company in connection with a reduction in its share capital.

National legal framework

The Law on dividend tax

3 Swedish legislation makes a distinction between resident and non-resident shareholders with regard to the taxation of payments to shareholders on the occasion of a repurchase of shares in connection with a reduction in a company's share capital. For resident shareholders, a repurchase of shares is taxed as a capital gain and the cost of acquisition of the repurchased shares can be deducted. The gain is taxed at the rate of 30%. For shareholders who are not resident in Sweden, however, the repurchase is treated as a distribution of a dividend and the cost of acquisition cannot be deducted.

4 The rules relating to distribution of dividends are set out in the Law on dividend tax (lag (1970:624) om kupongskatt, 'the 1970 Law'), which is applicable only to natural or legal persons who are not domiciled or permanently resident in Sweden ('non-resident shareholders').

5 Paragraph 1 of the 1970 Law provides that tax is to be paid to the State in respect of dividends declared on shares in Swedish limited companies. Under Paragraph 2(2) of the law, 'dividend' includes payments to shareholders, in respect of, inter alia, a reduction in share capital.

6 Under Paragraph 5 of the 1970 Law, dividend tax is deducted from the dividend at the rate of 30%, but that rate is often reduced in accordance with agreements for the avoidance of double taxation. Where the tax has been charged at a higher rate than that which ought to have been charged under such an agreement, there is a right to a refund under Paragraph 27 of the 1970 Law.

7 It is not permissible under that law to deduct the cost of acquisition of repurchased shares. Consequently, a shareholder who falls within the scope of that law must pay dividend tax at the rate of 30% on the whole share repurchase payment. Provisions in the double taxation agreement currently in force, however, can lead to a different outcome.

The Franco-Swedish double taxation agreement

8 The Agreement between the Government of the French Republic and the Government of the Kingdom of Sweden for the Avoidance of Double Taxation and the Prevention of Tax Evasion in respect of Taxes on Income and Wealth was signed on 27 November 1990 and entered into force on 1 April 1992 ('the Franco-Swedish agreement').

9 Article 10(1) of that agreement provides:

'Dividends from a company resident in one contracting State to a person resident in the other contracting State are taxable in the latter State.'

10 Under Article 10(2):

'Those dividends may also be taxed in the contracting State in which the company paying the dividends is resident, under the legislation of that State, but if the recipient of the dividends is the person actually entitled to them, the tax thus levied may not exceed 15% of the gross amount of the dividends.'

11 Under Article 10(5) of the Franco-Swedish agreement, 'dividend' means, inter alia, income from shares and income which, in the contracting State in which the company distributing the dividend is resident, is treated in the same way as a dividend under the legislation applicable when that agreement entered into force.

12 Under Article 13(6) of that agreement, a capital gain of the kind arising from the sale of shares such as those at issue in the main proceedings is taxable only in the contracting State in which the seller is resident.

13 That agreement is based on the Model Tax Convention drawn up by the Organisation for Economic Cooperation and Development (OECD), which also compiled commentaries on the model.

14 Point 28 of the commentary on Article 10 of the OECD Model Tax Convention states that payments regarded as dividends include not only the disbursement of profits decided at the annual shareholders' meeting but also other advantages with monetary value, such as bonus shares, bonuses, profits on liquidation and hidden dividends. The tax reliefs set out in that article are valid for as long as the State where the paying company is resident taxes such advantages as dividends.

15 Point 31 of the commentary on Article 13 of the OECD Model Tax Convention states that if a shareholder sells shares to the company that issued them, in connection with a liquidation of that company or a reduction in its share capital, the difference between the sale price and the nominal value of the shares may be treated as a distribution of accrued profits and not as a capital gain in the State in which the company is resident. That article does not prevent the company's State of residence from taxing such a dividend according to the tax rates laid down in Article 10 of the OECD Model Tax Convention. Such taxation is permitted because the difference is included in the definition of the expression 'dividend' in Article 10(3), as interpreted at point 28 of the commentary on that article.

16 According to the national court, the Franco-Swedish agreement, as interpreted in the light of the OECD Model Tax Convention and the commentaries thereon, brought about a change in the tax system established by the 1970 Law in that it fixes

the dividend tax rate for non-residents at 15% and permits an amount corresponding to the nominal value of the repurchased shares to be deducted.

The main proceedings and the questions referred for a preliminary ruling

17 On the occasion of a repurchase of its class B shares in connection with a reduction in its share capital on 2 December 1998, Ratos made a payment of approximately SEK 8 640 000 (EUR 917 000) to Ms Bouanich, resident in France. Tax was payable on the whole of that sum at 15%, that is, approximately SEK 1 300 000 (EUR 138 000), under the 1970 Law in conjunction with the Franco-Swedish agreement.

18 Ms Bouanich applied to the responsible tax office for a refund in respect, primarily, of the whole amount of the dividend tax paid and, alternatively, of that part of the dividend tax claimed on the basis of the nominal value of the repurchased shares.

19 On 28 September 1999, the tax office accepted her alternative claim and refunded to her the sum of approximately SEK 167 000 (EUR 18 000).

20 Ms Bouanich contested that decision before the Länsrätten i Dalarnas län (County Administrative Court for Dalarna), claiming that the outstanding dividend tax should be refunded to her. That claim was rejected by judgment of 29 March 2001, and she appealed against that judgment to the referring court.

21 Since it considered that the EC Treaty and the case-law of the Court of Justice did not provide any clear guidance on the answers to the questions that had arisen in the dispute before it, the Kammarrätten i Sundsvall (Administrative Court of Appeal, Sundsvall) decided to stay the proceedings and to refer the following questions to the Court for a preliminary ruling:

'(1) Do Articles 56 EC and 58 EC permit a Member State to tax a payment in respect of a share repurchase, paid out by a limited company in the Member State, in the same way as a dividend, without there being a right to deduct the cost of acquisition of the repurchased share, if the payment is made to a shareholder who is not domiciled or permanently resident in the Member State, whereas a share repurchase payment made by such a limited company to a shareholder domiciled or permanently resident in the Member State is instead taxed as if it were a capital gain, with a right to deduct the cost of acquisition of the repurchased share?

(2) If the answer to Question 1 is no: When the double taxation agreement between the Member State in which the limited company is resident and the Member State in which the shareholder is resident provides that there is to be a lower rate of taxation than that applied to a share repurchase payment made to a shareholder in the first Member State, and a shareholder in the second Member State, with reference to the commentaries on the OECD Model Tax Convention, is also permitted a deduction corresponding to the nominal value of the repurchased shares, do the articles mentioned in the previous question permit, in those circumstances, a Member State to apply a rule such as that set out above?

(3) Do Articles 43 EC and 48 EC permit a Member State to apply a rule such as that set out above?'

The questions referred for a preliminary ruling

Question 1

22 By its first question, the national court asks, in essence, whether Articles 56 EC and 58 EC must be interpreted as precluding national legislation, such as that at issue in the main proceedings, which provides that a payment in respect of a share repurchase to a non-resident shareholder in connection with a reduction in share capital is taxed as a dividend without there being a right to deduct the cost of acquisition of those shares, whereas the same payment made to a resident shareholder is taxed as a capital gain with a right to deduct the cost of acquisition.

23 Ms Bouanich submits that the 1970 Law constitutes a restriction on investment in Swedish companies by foreign investors and discrimination contrary to Article 56 EC, which cannot be justified even under Article 58 EC.

24 The Swedish Government does not dispute the alleged incompatibility between the 1970 Law and Community law. It accepts that the effect of the Swedish legislation on the tax treatment of payments in respect of a share repurchase is that tax-paying shareholders are treated differently according to whether they have limited or unlimited tax liability in Sweden. That tax system can therefore lead to a shareholder with limited tax liability sometimes being taxed more onerously than a shareholder with unlimited tax liability.

25 The government adds that it intends to amend that legislation so as to permit a shareholder with limited tax liability to deduct from a payment in respect of repurchased shares the cost incurred in acquiring those shares.

26 In the view of the Commission of the European Communities, it is clear that the Swedish legislation on the taxation of a share repurchase payment in connection with a reduction in share capital draws a distinction between resident and non-resident shareholders. The right to deduct the cost of acquisition of the repurchased shares amounts to a tax advantage which is not available to non-resident shareholders. That difference in treatment as between shareholders gives rise to discrimination in that analogous situations are treated differently, although there is no objective difference between the two situations such as to justify different treatment in that regard as between the two categories of taxpayers.

27 Consequently, the Commission considers that the discrimination which the 1970 Law gives rise to constitutes a restriction on the free movement of capital contrary to Article 56 EC. It appears from the order for reference that there are no circumstances capable of justifying such a restriction under Article 58 EC.

28 The first point to be noted here is that, according to the settled case-law of the Court, while direct taxation falls within the competence of the Member States, they must none the less exercise that competence consistently with Community law (see, in particular, Case C-80/94 *Wielockx* [1995] ECR-I 2493, paragraph 16, and Case C-319/02 *Manninen* [2004] ECR I-7477, paragraph 19).

29 A resale of shares to the issuing company such as that made by Ms Bouanich constitutes a capital movement as referred to in Article 1 of Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty (article repealed by the Treaty of Amsterdam) (OJ 1988 L 178, p. 5) and in the

nomenclature of capital movements set out in Annex I to that directive. This nomenclature still has the same indicative value for the purposes of defining the notion of capital movements (see Case C-452/01 *Ospelt and Schlössle Weissenberg* [2003] ECR I-9743, paragraph 7, and Case C-376/03 *D.* [2005] ECR I-5821, paragraph 24). A transaction of that kind therefore falls within the scope of the Community rules relating to the free movement of capital.

30 Article 56 EC prohibits all restrictions on the movement of capital between Member States, subject to the grounds of justification set out in Article 58 EC.

31 In order to answer the first question, it must first be ascertained whether a refusal by a Member State to allow a non-resident shareholder, on the occasion of a share repurchase, to deduct the cost of acquisition of the shares constitutes a restriction on capital movements.

32 In this connection, it should be noted that under the 1970 Law shareholders who have purchased shares in a Swedish company are subject to different rules according to whether or not they are resident in Sweden. Accordingly, a shareholder resident in Sweden is permitted, on the occasion of a repurchase of shares in connection with a reduction in share capital, to deduct the cost of acquisition of those shares, whereas a non-resident shareholder is not permitted to do so. The right to a deduction thus constitutes a tax advantage reserved solely to resident shareholders.

33 It is not disputed that such a tax advantage is, for those who enjoy the benefit of it, a form of tax relief and has the effect that non-resident shareholders, who are not able to enjoy that advantage, are taxed more onerously and therefore find themselves in a less favourable position than resident shareholders.

34 As the Advocate General pointed out at points 33 and 34 of her Opinion, the effect of such legislation is to make cross-frontier transfer of capital less attractive both by deterring investors who are not resident in Sweden from buying shares in companies resident in Sweden and also, consequently, by restricting the opportunities available to Swedish companies to raise capital from investors who are not resident in Sweden.

35 In those circumstances, it must be held that a refusal to allow a non-resident shareholder, on the occasion of a share repurchase, to deduct the cost of acquisition of the shares constitutes a restriction on the movement of capital within the meaning of Article 56 EC.

36 It falls next to be considered whether that restriction may be justified on any of the grounds provided for in Article 58(1) EC. It is clear from that provision read in conjunction with Article 58(3) EC that Member States may provide for a distinction to be made in their national legislation between resident and non-resident taxpayers, provided that such a distinction does not amount to a form of arbitrary discrimination or a disguised restriction on the free movement of capital.

37 As has already been noted in paragraph 34 above, the 1970 Law draws a distinction between resident and non-resident shareholders in that the payments they receive on the occasion of a share repurchase are taxed differently.

38 However, unequal treatment permitted under Article 58(1)(a) EC must be distinguished from arbitrary discrimination prohibited under Article 58(3) EC. According to the case-law, for a national fiscal provision such as that at issue in the main proceedings to be capable of being regarded as compatible with the provisions of the Treaty on the free movement of capital, the difference in treatment must

concern situations which are not objectively comparable or be justified by overriding reasons in the general interest (see Case C-35/98 *Verkooijen* [2000] ECR I-4071, paragraph 43; *Manninen,* paragraphs 28 and 29; and Case C-512/03 *Blanckaert* [2005] ECR I-7685, paragraph 42).

39 It must therefore be considered whether the different tax treatment of income received on the occasion of a share repurchase by resident and non-resident shareholders relates to situations which are not objectively comparable.

40 It must be noted that the cost of acquisition is directly linked to the payment made on the occasion of a share repurchase so that, in this regard, residents and non-residents are in a comparable situation. There is no objective difference between the two situations such as to justify different treatment on this point as between the two categories of taxpayers.

41 In those circumstances, national legislation such as the 1970 Law constitutes arbitrary discrimination against non-resident shareholders in so far as it taxes them more onerously than resident shareholders in an objectively comparable situation.

42 As regards the other grounds of justification provided for in Article 58 EC or in the Court's case-law, these were not relied on.

43 The answer to the first question must therefore be that Articles 56 EC and 58 EC must be interpreted as precluding national legislation, such as that at issue in the

main proceedings, which provides that a payment in respect of a share repurchase to a non-resident shareholder in connection with a reduction in share capital is taxed as a dividend without there being a right to deduct the cost of acquisition of those shares, whereas the same payment made to a resident shareholder is taxed as a capital gain with a right to deduct the cost of acquisition.

Question 2

44 By its second question, the national court asks whether the answer to the first question would be different where the tax system derives from a double taxation agreement, such as the Franco-Swedish agreement, which fixes a lower ceiling on the taxation of dividends for non-resident shareholders than for resident shareholders and, by interpreting that agreement in the light of the OECD's commentaries on its applicable model convention, permits the nominal value of those shares to be deducted from the share repurchase payment.

45 Ms Bouanich states that under the Franco-Swedish agreement the French Republic has the sole right to tax capital gains arising on a share repurchase transaction. The whole amount of the dividend tax wrongfully paid should therefore be reimbursed.

46 The Commission relies on the case-law relating to tax credits (Case 270/83 *Commission* v *France* [1986] ECR 2773) and tax benefits (Case C-307/97 *Saint-Gobain* [1999] ECR I-6161) in support of its submission that compliance with Community law cannot be dependent on the content of a double taxation agreement concluded between two Member States.

47 The Commission considers that a system, such as the one described in the main proceedings, applicable under a double taxation agreement and interpreted in the light of the commentaries on the OECD Model Tax Convention, is contrary to Articles 56 EC and 58 EC.

48 In that regard, it is necessary to consider whether the Franco-Swedish agreement must be taken into account in determining whether tax legislation is consistent with Community rules on the free movement of capital. If that is the case, it falls then to be established whether that agreement removes the restriction on fundamental freedom that has been found to exist.

49 It is to be noted that under the second indent of Article 293 EC, the abolition of double taxation is one of the objectives of the Community to be attained by the Member States. In the absence of unifying or harmonising measures at Community level for the elimination of double taxation, the Member States retain competence for determining the criteria for taxation on income and wealth with a view to eliminating double taxation by means, inter alia, of international agreements. In those circumstances, the Member States remain at liberty to determine the connecting factors for the allocation of fiscal jurisdiction by means of bilateral agreements (see Case C-336/96 *Gilly* [1998] ECR I-2793, paragraphs 24 and 30; *Saint-Gobain*, paragraph 57; and *D.*, paragraph 52).

50 None the less, such an allocation of fiscal jurisdiction does not permit Member States to introduce discriminatory measures which are contrary to the Community rules.

51 Since the tax system under the Franco-Swedish agreement, as interpreted in the light of the commentaries on the OECD Model Tax Convention, forms part of the legal background to the main proceedings and has been presented as such by the national court, the Court of Justice must take it into account in order to give an

interpretation of Community law that is relevant to the national court. It is not for the Court to interpret national law or to assess its application in the present case (see, inter alia, Case C-435/93 *Dietz* [1996] ECR I-5223, paragraph 39, and Case C-136/95 *Thibault* [1998] ECR I-2011, paragraph 21).

52 With regard to tax treatment under the Franco-Swedish agreement, it should be recalled that a non-resident shareholder such as Ms Bouanich is permitted, under that agreement, as interpreted in the light of the commentaries on the OECD Model Tax Convention, to deduct the nominal value of the shares from the taxable amount payable on the occasion of a repurchase of those shares. The remaining amount is then taxed at the rate of 15%.

53 In view of the fact that resident shareholders are taxed at the rate of 30% on share repurchase payments after deduction of the cost of acquisition, it must be ascertained whether those shareholders are treated more favourably than non-resident shareholders. In order to do this, it is necessary to know the cost of acquisition of those shares as well as their nominal value.

54 In that regard, it must be recalled that the assessment and finding of the facts in a case are not matters for the Court of Justice but for the national court (see Case 36/79 *Denkavit* [1979] ECR 3439, paragraph 12; Joined Cases C-175/98 and C-177/98 *Lirussi and Bizzaro* [1999] ECR I-6881, paragraph 37; and Case C-318/98 *Fornasar and Others* [2000] ECR I-4785, paragraph 31).

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

56 The answer to the second question must therefore be that Articles 56 EC and 58 EC must be interpreted as precluding national legislation which derives from a double taxation agreement, such as the Franco-Swedish agreement, which fixes a lower ceiling on the taxation of dividends for non-resident shareholders than for resident shareholders, and, by interpreting that agreement in the light of the OECD's commentaries on its applicable model convention, permits the nominal value of such shares to be deducted from the share repurchase payment, except where, under such national legislation, non-resident shareholders are not treated less favourably than resident shareholders. It is for the national court to determine whether that is the case in the specific circumstances of the main proceedings.

Question 3

57 In the light of the answers given to the first and second questions, it is not necessary to answer the third question.

Costs

58 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the national court, the decision on costs is a matter for that court. Costs incurred in submitting observations to the Court, other than the costs of those parties, are not recoverable.

On those grounds, the Court (Third Chamber) hereby rules:

1. **Articles 56 EC and 58 EC must be interpreted as precluding national legislation, such as that at issue in the main proceedings, which provides that a payment in respect of a share repurchase to a non-resident shareholder in connection with a reduction in share capital is taxed as a dividend without there being a right to deduct the cost of acquisition of those shares, whereas the same payment made to a resident shareholder is taxed as a capital gain with a right to deduct the cost of acquisition.**

2. **Articles 56 EC and 58 EC must be interpreted as precluding national legislation which derives from a double taxation agreement, such as the Agreement between the Government of the French Republic and the Government of the Kingdom of Sweden for the Avoidance of Double Taxation and the Prevention of Tax Evasion in respect of Taxes on Income and Wealth, signed on 27 November 1990, which fixes a lower ceiling on the taxation of dividends for non-resident shareholders than for resident shareholders, and, by interpreting that agreement in the light of the commentaries of the Organisation for Economic Cooperation and Development on its applicable model convention, permits the nominal value of such shares to be deducted from the share repurchase payment, except where, under such national legislation, non-resident shareholders are not treated less favourably than resident shareholders. It is for the national court to determine whether that is the case in the specific circumstances of the main proceedings.**

[Signatures]