

Chapter 7

The European Court of Justice and Direct Taxation: A Recent Change of Direction?

Mattias Dahlberg

7.1 Introduction

The importance of the fundamental freedoms of the EC Treaty for shaping the national tax system of the Member States cannot be enough emphasised. This is contrasted by the problems of the Council to reach the required unanimity to adopt common legislation in the field of direct taxation.¹

The general objective of this chapter is to examine whether, and if so to what extent, there have been major developments of the case law of the European Court of Justice, here also referred to as the Court. Because this field of law is based on case law, it is necessary to be relatively thorough when analysing the cases, especially recent cases.²

This chapter will examine some topical issues in the case law of the European Court of Justice in the field of direct taxation. Three main issues will be discussed. First, the Court's (possible) turn from a discrimination analysis to a restriction analysis. A highly related issue is the meaning of "objectively comparable situations", which is the second issue covered.³ Traditionally, the identification of objectively comparable situations has been the stepping stone for the discrimination analysis. Whether this still holds true will be subject to analysis. Third I will discuss grounds of justification in the general interest.

In relation to these three issues, three hypotheses will be tested.⁴ The first hypothesis is that regarding companies, the European Court of Justice has departed from a discrimination analysis to a restriction analysis. The second hypothesis is that regarding individuals the Court still upholds a discrimination analysis, whereby maintaining the requirement of identifying objectively comparable situations, even if anomalies exist in its case law. The third hypothesis is that the Court has become more amenable with regard to grounds of justification in the general interest.

In the final part of the chapter I attempt to make two alternative tax-policy explanations for the direction of the Court's case law identified. The first one is the cul-de-sac explanation, which means that negative integration through the case law of the Court has come to a point where it cannot go any further. Thus, the Court will continue to apply its previous case law, but it will not go beyond this

point. The second explanation is the U-turn explanation. According to this explanation the Court is now reversing its previous “integrationist” case law, permitting Member States a wider margin of sovereignty in the field of direct taxation.⁵

The chapter has the following outline. Section 7.2 gives a general background to the issues discussed. Fundamental freedoms and the meaning of discrimination are introduced. From a general perspective, the function of the European Court of Justice is also discussed. Section 7.3 deals with the meaning of “objectively comparable situations”. In a discrimination analysis it has been a precondition that the situations compared are “objectively” comparable. The meaning and development of this concept is discussed. Section 7.4 covers grounds of justification in the general interest. There are only a few grounds in the area of direct taxation that in principle have been accepted by the Court. Recent developments are considered, including the case C-446/03 *Marks & Spencer*. In the case C-374/04 *Test Claimants in Class IV of the ACT Group Litigation* the Advocate General (AG) Geelhoed in his opinion made an attempt outline a framework to the Court’s case law in the field of direct taxation. This structural attempt is subject to critical analysis in Sect. 7.5. A few cases that the European Court of Justice will decide in the future are discussed in Sect. 7.6. Concluding remarks are given in Sect. 7.7.

7.2 Background

It is clear that the fundamental freedoms of the EC Treaty prohibit restrictions, even if Article 39 on the free movement of workers refers to discrimination.⁶ “Discrimination” means the application of different rules to comparable situations or the application of the same rule to different situations. One relevant distinguishing criterion in the field of taxation is nationality.⁷ This form of discrimination is usually labelled direct or overt discrimination. Another form of discrimination is indirect or covert discrimination. This can be defined as the application of other criteria of differentiation that in fact lead to the same result, which also is relevant in tax-law cases.⁸

The first phase of case law from the European Court of Justice predominantly dealt with cases on discrimination. Moreover, the early cases dealt with infringement of fundamental freedoms that took place in the host state; the state where for example an establishment had been made. The second phase of case law in the field of direct taxation was instead focused on infringements taking place in the home state, the state where for example the investor was a resident. It seems as if the Court has stepped away from its previous discrimination analysis. Rather, the Court identifies whether the national measure at issue constitutes a “barrier” or likewise. This more vague language has been subject to criticism.⁹

A hallmark of discrimination is, as previously noted, that two situations are compared and one situation is treated worse than the other. In my view, it is possible to identify such comparable situations in a large number of cases where the Court has chosen to apply a restriction analysis.¹⁰

It has been debated whether or not the European Court of Justice takes political considerations when deciding its case law. For example, it has been suggested that