European Tax Law and International Tax Law*

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1. Introduction

In examining the relationship between European and international tax law, the first challenge is to delimit the research field: Does an international tax law exist? What are the components of European tax law? Only then can the relationship be analysed.

As far as international law is concerned, there are two possible conceptualisations. It can be seen either as the expression of the intention of nation States which, in order to build this system, agree to share part of their own powers, thus giving up part of their sovereignty; or as the implementation of pre-existing common principles. A combination of these two approaches can be used to explain the process of realisation of international tax law.

The next question concerns the shaping of the main characteristics of international tax law. The purposes of tax law include the legitimisation of taxes, the definition of their status and the organisation of their collection. Taxes are contributions paid in to the advantage of a public community, contributing to the definition of that community. The State is itself defined by its powers to raise taxes; these powers can be constitutionally recognised in relation to territorial communities when the State has a federal or decentralised structure. In addition, certain international organisations are, exceptionally, endowed with fiscal powers, especially the European Union, which receives customs duties, a share of VAT collected by Member States, and the taxes on its employees' income.

Starting from this observation, international tax law consists of two main components. The first component concerns the attribution and distribution

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of the fiscal powers of States to avoid any possible conflict. Since the actors are sovereign States, international tax law, as a branch of public international law, adopts the methods typical of public international law, that is to say international conventions that work on the basis of reciprocity. However, the techniques adopted by international tax law in order to avoid conflicts between the tax powers of sovereign States are those typical of private international law: the reference to the law of the State of residence and the choice of the *lex rei sitae* for the taxation of property are clear examples of this principle.

This key component of international tax law is undisputed. However, it should be noted that its dimension and relevance are minimal, since it does not exist on an international scale, except in the form of (mainly) bilateral agreements aimed at achieving a reasonable balance between national fiscal sovereignties. In other words, international tax law adopts solutions aimed at solving conflicts, but it does not implement any substantive provisions.

The second component of international tax law is more controversial than the first one, though its potential is significant. Our analysis starts with the search for possible standards of international tax law or, at least, of fundamental principles in international taxation, taking as the starting point the concept of equality in tax matters.

This perspective is to some extent chronological, casting light first of all on legal provisions adopted to avoid double taxation on consumption. Almost all States agree that goods should be able to leave the country of export without being taxed, then travel through transit countries in a condition of "tax suspension", and be taxed only in the country of final destination (i.e. the state of consumption). This unwritten rule is widely accepted because countries do not wish to hinder exports.

Direct taxation *lato sensu* (income tax, tax on company earnings, and property tax) is governed in a less universal manner. Bilateral conventions have been in place for decades, to the point that 3,000 of these conventions are now in existence, with "virtuous" States aligning their policies to the global fiscal compact. At the same time, several dozen countries have not concluded such conventions, thus to some extent "deregulating" the

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international tax playing field. In this connection an important role is played by the OECD, which has developed a model convention[2] the clauses of which are used by all contracting States, at least in their essential parts.

These conventions pursue three objectives. First of all, the prevention of double taxation (by virtue of which two taxes on the same asset are imposed on the same taxpayer). Double taxation is seen as a highly undesirable phenomenon, even though there are no rules stating the need for it to be eradicated. To this end, bilateral conventions stress the role of residence criteria in order to attribute the tax to one country rather than another.

The second objective is the prevention of dual non-taxation of taxpayers who try to escape taxes by managing their assets by means of cross-border operations. This objective may be considered to reflect the principle of equality before the public authorities, since the behaviour at issue results in the violation of the principle of equality between taxpayers. The principle of equality is undoubtedly of universal value, but its practical relevance was limited until recently due to the insufficient number of conventions and to the substantial non-application of provisions aimed at the realisation of this purpose. Since 2009, the provisions which have been put in place have become significantly more precise and efficient.

Traces of the principle of equality are to be found also in the third objective, that is, to combat discrimination based on nationality.

Considering the wide-ranging efforts of States based on these three main objectives, an image of an international tax law emerges which largely recognises, as a sort of *lingua franca*, a general theory encompassing the principle of the legality of taxes (the historical foundation of all regimes based on representation), respect for the ability to pay, equality before the public authorities and progressivity (by means of an effective global tax rate).

The questions posed by European tax law are less “existential”: European tax law does exist, but the identification of its main characteristics is complex. At first glance, it seems to be at the service of the Treaty, so that two aspects must be considered. First of all, a body of rules of substantive

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[2] OECD Model Tax Convention.

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law defines the tax regimes in terms of the objectives of the EU: a unified and totally European regime for customs duties, and a largely harmonised regime for taxes on consumption, i.e. VAT and excise duties. The EU has limited involvement in direct taxation, which is within the competences of Member States. However, the Court of Justice of the European Union has been asked to intervene in the name of the fundamental freedoms of the Treaty also in this sphere.

Thus, "hard law" and "soft law" co-exist. The co-existence of these two kinds of law, applicable to the territory of the EU, is complex, though it appears to be fairly efficient in managing the contemporary cross-border problems of tax law.

2. The traditional difference between the two legal orders

At first, the forms taken by international tax law and European tax law differ in that they reflect different aims and purposes, thus employing different technical provisions.

2.1 Differences with regard to the objectives pursued

International tax law exists in a largely functional perspective, while European tax law appears as one component of a legal system properly speaking.

2.1.1 The objectives of international tax law

A) *Ensuring the sovereignty of States*

Maxime Chrétien has argued that fiscal sovereignty is an international law principle with an essentially territorial character,[3] and foreign taxes are thus not applicable in the territory of the State, which enjoys a monopoly of taxation within its territory. The development of trade has disrupted this order and led to a cohabitation of sovereignties. Chrétien talks about "*droit international fiscal*" rather than "*droit fiscal international*", referring to a branch of public international law aimed at the protection of States. It is the result of historical sedimentation, parallel to the evolution of the movement of persons and goods, leading to a higher degree complexity of the tax

[3] CHRÉTIEN, M., *A la recherche du droit international fiscal commun*, Paris, Sirey 1955.

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system of each State, partly due to innovation by democratic regimes and partly due to the astonishing growth of the financial needs of States since the First World War.

The picture that emerges is of a system of international tax law created for contingency purposes in a chronological perspective. This is the case, first of all, with regard to customs duties (which are easy for States to institute and collect), constituting a matter for conciliation. The benefits accrued by way of cross-border trade take precedence over the collection of such revenue, thus leading certain countries to negotiate conventions which reduce or abolish customs duties by means of a "customs union", such as the Hanseatic League from the thirteenth to the seventeenth century and the *Deutsche Zollverein* from 1834 onwards.

There is also the matter of double taxation (that is to say the application of two taxes on the same asset held by the same taxpayer), which is seen as a counter-productive manifestation of State sovereignty that should be eliminated. The underlying intention is to avoid hindering the movement of persons and the exchange of goods with the application of two or more national tax regimes, which would result in taxation by multiple countries of the same tax base exclusively due to the fact that the tax base cannot be linked to only one state. Double taxation results from the simultaneous exercise of multiple tax sovereignties and becomes an "evil" to be eradicated not for reasons of fiscal justice, but efficiency, in the sense that each state has an interest in limiting its tax sovereignty in order to allow trade to prosper. This development of trade will then lead to the creation of more wealth and, as a result, a larger tax base. This idea has made its way in a pragmatic manner in the field of consumption tax, levied by all States: the aim of eliminating double taxation has thus become a key objective.

Almost all States agree on letting goods leave the exporting country without being taxed, and to be shipped in a condition of "tax suspension" across countries through which they are merely in transit, to be taxed only in the country of final destination (i.e. the state of consumption). Countries not wishing to penalise their exports, apart from a few isolated cases, accept this unwritten rule. Double taxation on consumer goods is thus eliminated and this practice is so widely accepted that it is possible to define it as part

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of customary law. However, this rule operates to the extent that States apply it and violations are not sanctioned.

In the historical perspective modern direct taxation (on income) first appeared in the nineteenth century, in the United Kingdom in 1848, in Germany in 1870, and in France in 1914-1917. In the case of income tax the risk of double taxation appears to be higher, since States pay closer attention to direct taxation, since the level of tax reflects the link with their citizens, an appeal to their ability to pay in democratic countries and the most visible expression of fiscal sovereignty.

Also in the case of income tax the prevention of double taxation appears to be necessary but harder to achieve. Some authors[4] consider the power of States to tax revenues to be part of international customary law by which countries can choose one of the following four criteria: nationality, domicile or residence, physical presence or an effective professional activity in the country, or alternatively the location in the country either of goods or of operations generating revenue.

This rule, without having the force of a legal provision or customary law, is largely accepted and many countries have adopted it on an exclusive basis for decades. In other words, countries have enacted legislation in light of these criteria, thus avoiding double taxation.

However, the development of trade and its growing complexity, together with the difficulty of achieving cross-border optimisation of tax systems and diminishing public resources, have led the majority of States in the international tax arena to enter into bilateral conventions.

The first steps of this process were taken in the nineteenth century (Convention between France and Belgium, 1843, Convention between the Second Reich and the neighbouring States, 1871), while the most important developments took place especially in the twentieth century, with an acceleration starting from 1960. In the vast majority of cases (3000 tax treaties have been concluded as of today), these conventions have been entered into on a bilateral basis. However, alongside these "virtuous" States

[4] GUSTAFSON, C.H., Peroni R.J., CRAWFORD PUGH R., "Taxation of international transactions", 4th edition, 2011, West, p. 16.

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there are some countries that have not concluded any such treaties, with the effect of "deregulating" the playing field of international taxation.

The scenario has become more homogeneous due to the influence of the OECD. Following the work of the League of Nations, since 1963 this organisation has adopted a model convention whose clauses are, at least as far as their basic principles are concerned, used by all contracting countries. These conventions pursue three objectives.

Clearly the first objective is to prevent double taxation, which is almost unanimously conceived as an objectively undesirable phenomenon. In order to eliminate it, all conventions search for a compromise between safeguarding national tax sovereignties and the need not to hinder trade, thus preferring the residence criterion in order to distribute powers to tax among States. The elimination of double taxation cannot be seen as a categorical imperative with universal value. States adhere to this principle to the extent that it is deemed to be useful, but they are not bound to it. At times they agree to adopt provisions maintaining a certain amount of double taxation.

The second objective is the avoidance of double non-taxation of taxpayers who try to escape the taxation normally applicable to them by managing their affairs transnationally. This objective is of a dual nature: from a technical point of view, it is about achieving a higher level of tax revenue in order to finance public expenditure; from a political perspective, it can be seen as reflecting the principle of equality vis-à-vis the tax authorities, since the behaviour at issue has the effect of upsetting the balance between taxpayers. This objective applies essentially to personal taxes (income tax, inheritance tax) in light of an underlying political agenda. Equality is a principle of universal value (no State can set aside the principle of equality in tax matters), but its practical value has so far been limited due to the insufficiency of tax conventions and the practical non-application of provisions aimed at achieving this objective. Since 2009, the provisions which have been put in place have significantly improved in terms of precision and efficiency.

The influence of the principle of equality can also be found in the third objective, which is the fight against discrimination based on nationality,

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summed up in the precept that two taxpayers of different nationality but both residing in the same country must be treated equally in cases in which their situations are identical. This principle is universally accepted, at least among States that have agreed to be bound by conventions. The dominant character of the liberal philosophy of the action of the UN works in the same direction.

Maxime Chrétien does not see any international tax law beyond this functional vision destined to safeguard national fiscal sovereignty. As of today, it is possible to cautiously envisage a wider dimension beyond this essential core.

B) *Moving towards the affirmation of common principles*

An idea emerges from the provisions adopted by States in relation to these three objectives, an idea of international tax law (reflecting fiscal problems arising out of cross-border situations encountered and/or created by taxpayers), which may serve as a sort of *lingua franca*, or general theory. It encompasses the principle of legality of taxation, respect for the ability to pay, equality before the public authorities, and progressivity (achieved by means of an effective global tax regime).

The principle of effectiveness can be combined with the democratic principle so that a democratic country and a totalitarian country can enter into a bilateral convention with provisions reflecting a balance between the State and the taxpayer, or at least limiting the possibility of arbitrary action of the State. In statistical terms several dozen States have signed a limited number of conventions without being tax havens. Each State is free to terminate a convention previously signed (see the case of Denmark, which, in 2009, renounced the conventions it had signed with France and Spain, or the case of France, which, in June 2014, renounced the 1953 convention on inheritance tax with Switzerland), but the solutions they adopt after re-establishing their full sovereignty remain in line with the picture outlined by Gustafson and Peroni. This shows that the scope of international tax law is wider than that described by Chrétien.

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2.1.2 The ambitions of European tax law

A) *Ensuring the realisation of the objectives of the Treaty*

European tax law is conceived as part of a supranational juridical system. As such, within its areas of competence, it pursues the objectives of the Treaty, but it also contributes to the surveillance of national tax regimes.

The different provisions (Treaty and secondary law) dealing with tax are part of the system constituting European law and they are part of this system to the extent that they serve the purposes of the EU and contribute to the realisation of the Internal market while safeguarding the fundamental freedoms established by the Treaty. In other words, tax provisions are, as in any national system, a specific part of a coherent political entity ensuring the functioning of the public administration within its territory.

Customs duties were the first category of tax to be unified by EU law. Articles 28-33 TFEU governing the circulation of goods introduced a standard system of taxation in States importing goods. After the adoption of common customs tariffs by the EU, within the framework laid down by the World Trade Organization (WTO), the collection of customs duties (which constitute a resource for the EU budget) depends on administrative cooperation between the authorities of the Member States.

Other taxes harmonised by the EU are turnover taxes, that is to say Value Added Tax and excise duties. This revenue essentially remains part of the Member States' own resources (except for the share of VAT received by the EU), but the essential characteristics of the regime were laid down in Article 113 TFEU with the aim of realising the Internal market. Several directives regulate these matters: for VAT in particular the essential provisions are laid down in the Sixth Directive,[5] consolidated by Directive 2006/112/EC.[6] For excise duties on alcohol, tobacco and energy, the general regime is established by Directive 2008/118/EC.[7]

For the purposes of harmonisation of these two kinds of tax, Member States are required to transpose the EU Directives into their own national legislation. As a result, as of today, the tax regime for turnover taxes consists of 28 families of national tax regulations, 80% of which are

[5] Directive 77/388/EEC, 17 May 1977, OJEC, L 145 of 13 June 1977.
[6] Directive 2006/112/EC, 28 November 2006, OJEC, L 347 of 11 December 2006.
[7] Directive 2008/118/EC, 16 December 2008, OJEC, L 9 of 14 January 2009.

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identical for all countries in terms of their field of application, the definition of the tax base, and the right to deductions. The general framework for the evolution of such taxes is established by Article 113 TFEU, which provides for a specific intervention of the Council to approve legislation by unanimous vote after consulting the European Parliament and the Economic and Social Committee, in order to pass new harmonisation measures.

Other taxes are not included to the same extent within the competences of the EU. Article 293 (formerly Article 220) of the Treaty compelled Member States to engage in negotiations in order to ensure the elimination of double taxation within the EU, with a sort of "obligation of means" which had no application in the field of direct taxation and was repealed by the Treaty of Lisbon. The provisions of the TFEU are less stringent: reference is made essentially to Article 115 TFEU, which calls for the promotion by the Council by unanimous vote of a *rapprochement* of national provisions where they have a direct influence on the establishment and functioning of the Internal market. The legislative framework of the EU is therefore much more limited with regard to taxes that are left to the competence of the member States.

With regard to personal income tax, the only relevant provision is the Directive on taxation of income on savings in the form of interest payments,[8] setting out a system of exchange of information between administrations by means of which each authority communicates to other corresponding authorities the identity of their nationals with an account on their territory and the amount of interest generated by this account on a yearly basis. This communication is temporarily replaced by a withholding tax by States due to the constitutional protection of bank secrecy in certain States (Austria, Belgium and Luxembourg). This provision has been undergoing a process of evolution since the Council adopted a modification aimed at enlarging its field of application, thus making it compulsory to exchange information for natural persons,[9] while the fight against tax avoidance launched by the OECD together with the G20 has compelled the three States granted the above-mentioned derogation to repeal their system of withholding tax.

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[8] Directive 2003/48/EC, 3 June 2003, OJEC, L 157/38 of 26 June 2003.

[9] Directive 2014/48/EU, 24 March 2014, OJEU, L 111/50 of 15 April 2014.

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Tax on company earnings was affected by the EU in 1969 with the adoption of a directive which addressed the issue in a collateral manner, instituting and harmonising indirect taxes on the raising of capital.[10]

Many proposals by the Commission have encountered the opposition of the Council, but a significant legislative change took place on 23 July 1990, when two directives and a multilateral convention were adopted. Directive 90/434[11] deals with the tax regime of mergers, divisions and transfers of assets, requiring all Member States with a favourable regime to grant it not only for internal operations, but also for operations concerning companies of another Member State. This provision was modified in 2005[12] in order to include new forms of companies.

The second provision adopted on 23 July 1990 is the directive on the common tax regime applicable to parent companies and subsidiaries of different Member States.[13] In the same spirit, this law does not set up a comprehensive tax regime, but requires Member States that grant an exemption for dividends that a parent company receives from its subsidiary (for reasons of tax neutrality within integrated groups) to extend it also to cases where dividends are paid by a subsidiary with a registered office in another Member State. The field of application of this directive has been expanded[14] and a new directive[15] adapting the rules to current necessities replaced the two provisions.

The Commission realised that this new draft dealt only with certain kinds of erosion of the tax base by way of cross-border operations. It therefore proposed the adoption of a new directive aimed at preventing a parent company located in a third country from bypassing withholding taxes imposed by the Member State where its subsidiary is located by way of interposition of another subsidiary with its registered office in a Member State not applying withholding taxes.[16] This proposal is based on the adoption of a common anti-tax evasion rule but it has not yet been

[10] Council Directive 69/335, 17 July 1969, replaced by Directive 2008/7/EC, 12 February 2008, OJEU L/46/11 of 21 February 2008.
[11] Directive 90/434/EEC, 23 July 1990, OJEC, L 225 of 20 August 1990.
[12] Directive 2005/19/EC, 17 February 2005, OJEC, L 58/19 of 4 March 2005.
[13] Directive 90/435/EC, 23 July 1990, OJEC, L 225 of 20 August 1990.
[14] Directive 2003/123/EC, 22 December 2003, OJEC, L 07/41 of 13 January 2003.
[15] Directive 2001/96/EU, 30 November 2011, OJEC, L 345/8 of 29 December 2011.
[16] Proposal of Council Directive, 25 November 2013, COM(2013), 814 final.

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adopted. These legislative measures aim at realising a vast internal market for enterprises where competition is not altered by national tax provisions.

The third provision adopted on 23 July 1990 is a simple multilateral convention setting up an arbitration procedure to resolve disputes between companies from different Member States and their respective tax administrations in cases in which one of the administrations adjusts the tax base applying transfer pricing rules. The conditions laid down for the application of this procedure reduce it to a merely theoretical role in the context of transfer pricing issues and to a lesser position than that of the Joint Forum on transfer pricing, a simple structure where national authorities and representatives of taxpayers meet in a manner which appears to be fairly effective.[17]

In addition to this substantial, though isolated, package, the EU legislation on company taxation is limited, the only provision worthy of mention being a directive aiming at the abolition of all withholding taxes on interest and royalties between associated enterprises.[18] There are no EU provisions on capital gains tax or inheritance tax.

Other provisions aim at improving the exchange of information between tax authorities. The first provision was a 1977 directive[19] that was replaced by Directive 2011/16/EU,[20] as part of the more global – and probably more restrictive – framework imposed by the OECD multilateral convention, the signing of which in now in process. The other provision is a directive on mutual assistance in the field of recovery of tax credits, the purpose of which is to achieve a higher level of cooperation. In this way a Member State does not need to get involved in procedures for the recovery of taxes against a taxpayer in another Member State, but can ask for the assistance of the other Member State to implement an executive order taken by its own authorities (administrative or judicial).[21]

[17] Commission Decision 2007/75/EC.
[18] Directive 2003/49/EC, 3 June 2003, OJEC, L 157 of 26 June 2003.
[19] Directive 77/799/EC, 19 December 1977, OJEC, L 336, 27 December 1977.
[20] Directive 2011/16/EU, 15 February 2011, OJEU, L 64/1 of 11 March 2011.
[21] Directive 2010/24/EU, 16 March 2010, OJEU, L 84/1 of 31 March 2010.

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European tax law is not limited to the adoption of the above-mentioned substantive provisions, but is also intended to supervise the tax legislation of all Member States.

B) O*rganising the supervision of national tax regimes*

This second policy objective of European tax law is in accordance with the specificity of EU law, but a distinction must be made between two cases.

In the first case the supervision focuses on how Member States transpose and/or apply EU law on taxation. This is the prerogative of the Commission, which can bring infringement procedures before the Court of Justice of the European Union. The Court's approach is a cautious one, as the Court prefers a negotiation procedure with the State concerned, and the procedure may last for a long time.

As a result, the Commission has realised, in relation to the *Marks & Spencer* case,[22] that the British group relief regime (that is to say the possibility of offsetting the losses from a subsidiary against the profits of the group) was not in line with the freedom of establishment, totally excluding the possibility of offsetting the losses of subsidiaries located in other Member States. The United Kingdom refused to accept this case law and to modify its regime, in spite of the fairly balanced view adopted in the judgment. After having ruled out the possibility of negotiations with the UK, the Commission filed an infringement procedure.

The Court was also called on to rule on the case of preliminary referrals, thus explaining the relevance of a certain provision of European tax law with regard to a specific case (for example, the notion of turnover tax).[23]

The intense activity of the CJEU resulted in the Court becoming a sort of "substitute legislator", since EU law provisions are not subject to a process of implementation due to the paralysis of Council decision-making resulting from the unanimity rule. A paradigmatic case is that of Value Added Tax (VAT), which is 80% harmonised and accounts for between 25% and 45% of the tax revenues of the Member States, but also a tax regime based on provisions that are almost 40 years old. Following a preliminary referral, it

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[22] Court of Justice of the European Union, 13 December 2005, C-446/03, *Marks & Spencer*.

[23] Court of Justice of the European Union, 3 October 2006, C-475/03, *Banca popolare di Cremona*.

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is up to the Court to resolve the conflicts of interpretation between tax administrations and taxpayers, thus determining the field of application of VAT with regard to contemporary economic circumstances that could not be envisaged by the legislator in 1977.[24]

The accomplishment of such a task leaves almost all the parties somewhat dissatisfied, starting from the Court that promotes its own view of justice, while protesting against the instrumental use of the inactivity of the Council, since *de minimis non curat praetor*. Also on the part of the Commission there is a certain amount of dissatisfaction with the adoption of "soft law" which is difficult to govern because it embodies only certain strands of the Court's judgments. There is dissatisfaction also on the part of the taxpayers and the tax authorities, since the rules seems to lack clarity and simplicity.

The second case is subtler, more original and more remarkable. In the field of direct taxation, which is jealously defended by the Member States, the CJEU is required to examine whether national provisions concerning a domain that is left to the full competence of Member States complies with the fundamental freedoms of the Treaty. The activity of the Court in this case is unusual, since the Court has responded to the requests of national judges and the Commission to hand down an opinion in a field which is not intrinsically part of European tax law, to ascertain whether national regimes comply with the freedoms established by the TFEU, with the repeal of such regimes by the national legislator in cases in which the provisions fail to comply with the Treaty.

This extension of European tax law is built on a void, since it cannot lead to the setting up of a tax regime in the field of direct taxation, yet it results in the construction of a corpus of prohibitions weighing heavily on the actions of national legislatures. The difference with international tax law therefore takes many forms and has an impact on the provisions that each national regime adopts.

[24] For the exemption of services relating to sports activities, see Court of Justice of the European Union, 19 December 2013, C-495/12.

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2.2 Differences in terms of the provisions employed

2.2.1 The provisions employed by international tax law

The technical provisions employed are substantially different. International tax law gives precedence to the use of conventions, especially bilateral ones, and adopts a method grounded on safeguarding state sovereignty.

2.2.1.1 The precedence given to international conventions

Traditional international tax law gives precedence to bilateral conventions as instruments to achieve objectives which are functional to the ends pursued, notably the prevention of double taxation. They are classical international treaties whose adoption is regulated by public international law: negotiation, signature by the High Contracting Parties and ratification (at least in the dualist theory) to become law, generally ranking below national constitutions but above ordinary legislation.

Certain courts, starting from the French *Conseil d'Etat*, have ruled that the pre-eminent role of regularly ratified conventions does not correspond to the significance of their content. In a ruling handed down in 2002, the *Conseil d'Etat* described the paradox of this situation by showing that the exalted status given to international conventions within the hierarchy of provisions does not entail absolute predominance over French law, and that this predominance only serves the purposes of the conventions, that is to say the prevention of double taxation. On the contrary, conventions give way to provisions concerning the applicable fiscal regime:

"*In light of the fact that, if a bilateral convention signed in order to prevent double taxation is, according to Article 55 of the Constitution, able to take precedence, on this or that point, over tax law, the same convention cannot, however, directly serve in itself as a legal basis for a decision concerning tax; that, consequently, it is up to tax judges, in case of an issue concerning such convention, to first look at national tax law in order to understand whether the tax at issue had been regularly imposed and, in case of affirmative answer, on which grounds; that it is also up to tax*

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judges to determine, in approaching the analysis of the convention… whether or not said convention prevents national tax law from applying".[25]

In other words, tax conventions are sources of tax law that are pre-eminent because of their status and, at the same time, subsidiary with regard to their content, since they necessarily refer to criteria and definitions deriving from national law. It should also be noted that this analysis has been developed by the *Conseil d'Etat* in a systematic manner, even with regard to cases in which the convention at issue has its own definitions and criteria: in such cases, its position can therefore be contested.[26] The courts allow the application of the convention to put the taxpayer in a comparatively worse situation.[27]

The OECD has adopted two model conventions that are regularly updated: one dedicated to tax on income (*lato sensu*) and capital, the latest version of which was published in 2014, and one dedicated to inheritance tax, which dates back to 1982. The first one is by far the most important, having served as the basis for the adoption of almost 3000 conventions, whereas the second one has been used only in approximately 150 cases. For this reason the first model convention is of particular interest in our analysis.

In order to achieve each of the three objectives, bilateral conventions on the taxation of income and capital adopt the techniques advocated by the OECD Model Convention.

A) With regard to the prevention of double taxation (which is the oldest and most important of the objectives), conventions employ three different means. First of all, they adopt common definitions, grounded in almost every case on a common principle, the principle of territoriality, (with some notable exceptions, e.g. the United States, which refers to nationality instead). In addition they adopt a common method, starting from the territoriality principle, making it possible to determine which of the two countries involved receives the tax revenue from a certain tax base. In this

[25] *Conseil d'Etat*, 28 June 2002, *Schneider Electric*, 232276.

[26] *Conseil d'Etat*, 11 April 2008, *Cheynel*, 285583, on the Convention between France and Belgium.

[27] *Conseil d'Etat*, 12 March 2004, 362528, Sté Céline, concl. Aladjidi, note Ph. Durand, in Rev. Dr. Fisc. 2014/22, comm. 356.

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way, for each of the taxes concerned, conventions define the criteria resulting in the prevention of double taxation: either the State of residence of the taxpayer or the State of the source for income tax, the State where the immovable asset is located for capital gains tax, and the State of last domicile for inheritance tax.

Each criterion is then broken down into sub-criteria the use of which makes it possible to deal with each case of possible double taxation. Thus, for the residence criterion, conventions rely on the definitions adopted by each national regime, showing the merely functional nature of these rules and the fact that they cannot *per se* be seen as part of a legal system. However, in cases in which a taxpayer may be considered as resident in each of the States involved by applying domestic provisions, then and only then will conventions apply their own criteria (place of effective interest, place of vital interests, place of main dwelling and, finally, nationality) in order to consider the taxpayer as resident, for fiscal purposes, in only one of the two countries, thus preventing double taxation.

Exceptionally, some conventions define their own residence criteria, without making reference to national definitions (e.g. the convention between France and Belgium, and the convention between France and Libya).

Each convention provides for its own system of attribution of tax revenue to one of the two States and also for the possibility for the tax authorities of the States to exchange information in their possession to ensure a more effective implementation of the convention and improve the recovery of national taxes.

B) The prevention of double non-taxation employs its own methods, the characteristics of which are less precise and which vary considerably from one convention to another. The conventions basically put in place procedures for the exchange of information, which can either be automatic, spontaneous or on request (in which case the exchange of information can be limited in practice by constitutional norms such as bank secrecy).

These procedures have undergone profound changes in recent years, due to diminishing public resources and the subsequent attempt by States to improve tax collection.

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The reluctance of some States to respond to requests from other States is a reflection of two developments.

The first is the entry into force in the US on 1 July 2014 of the Foreign Account Tax Compliance Act (FATCA). These rules require foreign financial institutions to report to the US Treasury all accounts held by US citizens and the state in which they are located. The legislation has a worldwide scope of application and provides for dissuasive sanctions, thus leaving other States no choice but to comply, at best by signing a protocol setting out how this reporting obligation is to be implemented and enforced.[28] The strength of the US legislation has had an impact even on the most reluctant countries.

This new legislation, together with the 2008 financial crisis and the conclusions reached by the London G20 meeting of April 2009, has given impulse to the adoption of a multilateral convention concerning the automatic exchange of information among tax authorities. Since its inception, this exchange of information has been carried forward as a joint effort of the Council of Europe and the OECD.

Following the impulse given by the G20 (Cannes, 2011), the OECD has produced a new convention and proposed its adoption, and it has now been signed by more than 80 countries (including Andorra, Ireland, Kazakhstan, Liechtenstein, San Marino, Singapore and Switzerland). The ratification process is underway and States have agreed on how the exchange of information is to be put in place. In addition in 2014 the OECD submitted the rules on automatic exchange of information concerning tax matters for the approval of the G20.

From 2017 onwards, the step forward is going to be substantial, with a multilateral convention whose adoption process has been accelerated by the budgetary and financial events affecting most States since 2008.

C) The elimination of discrimination based on nationality is ensured, in the international tax law framework, by the provision contained in Article 24 of the OECD Model Convention, that is generally transposed into bilateral conventions in its entirety.

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[28] This Protocol was signed on 5 February 2012 by France, Germany, Italy, Spain and the United Kingdom.

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According to this provision, national tax regimes must apply an identical treatment to identical situations, and different rules in cases in which the situations of two taxpayers are different. The highest level of protection is granted when the provisions apply even when the national of the other contracting state resides in a third country.

This kind of protection is illustrated by the judgment in the *Biso* case, rendered by the French *Conseil d'Etat.*[29] In this case the judges ruled that according to the conventions signed by France and the respective countries, an Italian national and a British national residing in Monaco should be treated in the same way as a French national residing in Monaco are treated in accordance with the terms of the convention between France and Monaco. As a result, tax on income from their property located in France should be applied, and not the derogatory regime provided in Article 164 C of the *Code Général des Impots*.

Article 24 is certainly applicable, but in cases in which all States involved are members of the European Union, two similar provisions can take precedence: Article 14 of the European Convention on Human Rights[30] and Article 18 TFEU. Whereas the first provision is an example of "classical" international law applied to tax matters, the second one is an expression of "pure" European law.

2.2.2 Provisions employed by European tax law

The provisions employed by European tax law operate according to a different perspective, that is to say the perspective of a specific legal system. The first provision relies on the principle of general prevalence, upheld by the Court since 1962: "the EEC Treaty takes precedence, with regards to the subject that it regulates, over conventions signed before its entry into force between Member States".[31] This prevalence applies equally to secondary law (directives and regulations), with direct effect. In these conditions, tax law provisions that are part of EU law substantially contribute to the fiscal regime applicable in each Member State, where it applies to taxpayers and tax administrations.

[29] *Conseil d'Etat*, 11 June 2003, 221075, *Epoux Biso*.
[30] Article 14 of the European Convention on Human Rights.
[31] Court of Justice of the European Union, 27 February 1962, *Commission v. Italy*, 10/61.

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The difference is one of scope, which effectively reflects the essential distinction in the nature of these two types of provisions relevant to cross-border tax arrangements. CJEU case law has significantly improved over the years, taking account of the interface with private international law,[32] but when it is called to mediate between subsidiarity and implicit competences, notably with regard to new Member States bound by conventions signed prior to accession to the EU which are in contrast with the competences of the EU, its reaffirmation of the prevalence of EU law is certain and unambiguous.[33]

The second provision is part of the framework shaped by the first provision. In the domain of competences attributed by the Treaty and in light of the above-mentioned principle of precedence, the provisions employed by European tax law are those of an original legal system, more integrated as a national juridical system than the traditional system of public international law.

The applicable framework is not expressly specified by European tax law provisions, but its effective functioning, the direct effect of certain provisions, the obligation for States to transpose directives into their legal systems (the limited number of regulations in tax matters) and the almost absolute precedence of Treaty freedoms over national tax provisions are ensured and controlled by the Commission, either spontaneously or at the request of taxpayers or another Member State, with the possibility of submitting the case to the Court of Justice of the European Union. This competence includes the possibility to sanction a Member State that has failed to comply with a judgment handed down by the Court on infringement.[34]

The CJEU can also receive requests for annulment of an act promulgated by an institution of the EU which supposedly infringes EU law: for example, the Court rejected the request for annulment made by the United Kingdom against the decision of the Council which, in January 2013, had authorised a

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[32] Court of Justice of the European Union, 14 October 2008, C-353/06, *Stefan Grunkin*, with the Conclusions of AG Sharpston, §37-46.

[33] Court of Justice of the European Union, 3 March 2009, C-205/06 and C-249/06, *Commission v. Austria* and *Commission v. Sweden*.

[34] Court of Justice of the European Union, 13 May 2014, C-184/11, *Commission v. Spain*.

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procedure of enhanced cooperation in the field of taxation on financial transactions.[35]

The difference with international tax law is self-evident and stressed even further by the need to serve the interests of the States. As a result, the day-to-day practice of the actors of this legal system shows an increasingly high level of interpenetration.

3. A growing contemporary interpretation

The rule of law leaves unsolved two types of concerns, which are objectively opposed: on the one hand, the attempt by all national tax administrations to maximise their tax revenues, and on the other hand the attempt by taxpayers to minimise their tax liabilities. The first reflects the need to serve the general interest, while the second may be unlawful. The need for social stability gives rise to the need to reconcile these two concerns by means of provisions organising the substantive background and procedures in the tax field.

In a continent such as Europe with a long-standing juridical tradition there may be a certain amount of redundancy between rules established by a bilateral convention, rules established by EU law, and rules established by the European Convention on Human Rights. The above-mentioned example of the principle of non-discrimination on grounds of nationality is useful to illustrate this point. The tax authorities and the courts are called on to establish the applicable rules and how they are to be implemented, and the Court of Justice of the European Union is called on to monitor the functioning of this system, establishing rules of coexistence between the two legal orders and defining procedures to handle contemporary cross-border tax issues.

[35] Court of Justice of the European Union, 20 April 2014, C-209/13, *United Kingdom v. Council*.

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3.1 The rules of coexistence posed by the Court of Justice of the European Union

International conventions and EU law work on different levels. However, their implementation relies on hierarchical relationships which lead the CJEU to sanction possible influences of international tax law on Treaty freedoms.

3.1.1 A distribution of competences based on the scope of application in a hierarchical relationship

If there is an international tax law, it is defined first of all by its function. The CJEU underlines the fact that bilateral conventions, which are under the influence of the OECD (at least in conceptual terms), serve to ensure the elimination of double taxation[36] according to their own procedures and, therefore, the limits that the High Contracting Parties intended to lay down.
In the *Gilly* case, the CJEU stated that this role played by international tax law is not affected by EU law, since States have not made any use of Article 293, which, before being cancelled by the Treaty of Lisbon, allowed them to adopt harmonisation measures in the field of direct taxation. The Commission encouraged the Court to recognise that "direct taxation is not an exclusive competence of member States, being implicitly and necessarily included within the competences with regard to the internal market according to Article 4, par. 2, of the TFEU and considered as a competence which is shared between the European Union and member States".[37]
Consequently, the Court rejected the request of a Belgian taxpayer objecting to the excessive level of tax on dividends paid in France compared with the tax treatment of dividends paid in Belgium as a result of the convention between France and Belgium.[38]
A convention can also ignore certain consequences in terms of double taxation deriving from the parallel exercise by the States of their respective fiscal competence.[39]

[36] Court of Justice of the European Union, 12 May 1998, C-336/96, *Gilly*.
[37] Court of Justice of the European Union, 6 June 2013, C-383/10, *Commission v. Belgium*.
[38] Court of Justice of the European Union, 16 July 2009, C-128/08, *Damseaux*.
[39] Court of Justice of the European Union, 10 February 2011, C-436/08 and C-437/08, *Haribo*; Court of Justice of the European Union, 19 September 2012, C-540/11, *Levy & Sebbag*.

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In other words, traditional international treaties aim to regulate cross-border taxation and the Court recognises their exclusive competence in this regard, since the Council has not (unanimously) decided on harmonising either income tax or the prevention of double taxation. As a result, it is as sovereign States and international law subjects that Member States of the EU organise on a bilateral basis the mechanisms to prevent double taxation, *lato sensu*, without EU law being in the position to sanction any violation of this conventional law by one of the signatories.[40]

This system is incomplete, since not all the 310 bilateral conventions required to cover relations between the 28 Member States have been negotiated: for example, there are no conventions between Greece and Portugal, between Spain and Denmark, or between France and Denmark.

The reference to the OECD model convention gives treaties a fairly homogeneous character, but these conventions remain the result of full sovereignty. It follows that their contents vary in relation to the physical and economic characteristics of the two contracting parties: some of them, for example, contain provisions on border workers, and the provisions adopted to eliminate double taxation differ significantly. At the same time, the effect of the advantages given to nationals of the other contracting State may differ from one convention to another, even though they have both been negotiated by the same State. These advantages can result in a substantial advantage for third-country nationals. Member States are not obliged to grant other EU Member States the conditions of the most-favoured-nation clause. On the other hand, in cases where a treaty provision clashes with a provision of EU law, the CJEU states that the joint participation of the two legal orders to achieve the same objectives is still of a hierarchical nature.

3.1.2 Member States’ freedom in negotiation is conditional upon compliance with EU law

EU law applies to the part of tax law within the competences established by the Treaty, thus limiting the possibilities of Member States to enter into bilateral conventions for the elimination of double taxation. The CJEU case

[40] Court of Justice of the European Union, 19 September 2012, C-540/11, *Levy & Sebbag*.

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law follows the path laid down by all the treaties concluded by the Member States. This case law distinguishes between treaties signed before and after accession to the European Union, while always stating the prevalence of EU law. However, the Court has established that a Member State cannot use accession to the EU as a pretext to avoid the obligations deriving from a treaty concluded with third countries, at least when the treaty was signed before accession to the EU. Third countries are not entitled to the same level of protection when entering into an agreement with a state that was known to be part of the European Union.

CJEU case law starts from the *Commission v. Italy* case and has undergone a remarkable development with regard to implicit competences (or, at least, competences not yet exercised by the European Union) with the cases *Commission v. Austria* and *Commission v. Sweden*. The Court has not examined conventions signed by Member States with other States concerning tax harmonisation. In this connection, it has only had to intervene with regards to national provisions.

With regard to bilateral tax conventions, the Court adopts a twofold approach in order to ensure compliance with the fundamental freedoms.

First of all, it does not hesitate to define national provisions implementing the content of a bilateral convention as failing to comply with the free movement of capital, stating that:

"*Articles 56 and 58 EC must be interpreted as preventing national provisions resulting from a convention for the elimination of double taxation such as the convention between France and Switzerland*".[41]

It would be difficult for the Court to be any clearer than this on the hierarchical relationship between the two legal orders.

Second, the Court aims to ensure an effective implementation of Treaty freedoms by Member States. Consequently, if strict implementation of a bilateral convention leads to the validation of a discriminatory national provision, this gives Treaty freedoms a value that goes beyond conventional limits to allow for the national provision to be declared as non-compliant with the Treaty.

[41] Court of Justice of the European Union, 19 January 2006, C-265/04, *Bouanich*.

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Thus, the Court deals with the intertwining between bilateral conventions and European provisions by showing the value that the Treaty is supposed to add to conventions, even though this falls within the competences of Member States and, therefore, within the scope of conventions.

The most significant case with regard to this evolution is *Schumacker,*[42] in which the Court ruled that German law failing to grant the conditions granted to residents also to a non-resident whose income was for the most part from German sources hinders the effective implementation of the freedom of movement of workers for a Belgian citizen residing with his family in Belgium while working in Germany. The application of the provisions of the convention between Belgium and Germany would have made him "fiscally invisible", since his family circumstances would have been taken into account neither in Belgium (where his income was too low to be considered for tax purposes) nor in Germany (where the law granted this benefit to residents only). The convention was overruled in this case, because its literal implementation would have led to partially deprive one of the fundamental freedoms of its effects. The very practical approach of the Court in this case enhanced the effectiveness of the protection granted to taxpayers by a Treaty freedom in a field which does not fall within the competences of the EU (and, in doing so, the Court highlighted the precedence of EU law). In order to take this ruling into account, German law had to be modified, providing for benefits granted to German residents to apply in all cases where at least 90% of a taxpayer's income comes from German sources.

It should also be noted that the Court has taken other treaties into consideration in order to evaluate the validity of a national provision in the field of direct taxation: for example, the Convention signed between the United Kingdom and Switzerland on the free movement of persons[43] was used as a parameter to establish that a decision by the German tax authority denying German nationals resident in Switzerland the benefits that German law grants resident taxpayers was not compliant with EU law.[44]

[42] Court of Justice of the European Union, 14 February 1995, C-279/93.

[43] Convention between the United Kingdom and Switzerland on the free movement of persons, signed in Luxembourg, 21 June 1999, OJ 2002, L 114, p. 6.

[44] Court of Justice of the European Union, 28 February 2012, C-425/11, *Ettwein*.

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In addition, the EEA Agreement[45] was cited to establish that a Belgian tax imposed only on non-resident banks was contrary to the free movement of capital, thus leading the Court to consider the relevant provisions as violating Articles 56 and 63 TFEU, but also Articles 36 and 40 of the EEA Agreement.[46]

Adopting a similar reasoning, the Court found the Belgian tax regime granting a tax rebate for contributions paid in connection with pension schemes only to institutions established in Belgium was contrary to the freedom of establishment provided for in Article 56 TFEU,[47] thus limiting the scope of the justification based on the coherence of the tax system established by the *Bachmann*[48] and *Commission v. Belgium*[49] cases.

Through the role of the Court as interpreter and defender of the Treaty freedoms, its case law has had an impact on the tax regime hitherto resulting from the combination of national law and bilateral conventions. As a result, national legislatures and the High Contracting Parties have become aware of the need to integrate European law into the process of drafting tax regimes.

The Court recognises an *a posteriori* right to justify the limits placed to one or the other Treaty freedom by a national tax provision in light of a pre-eminent reason of general interest, on condition that the provision at issue is proportionate to the aim pursued (that is to say, the provision should limit the Treaty freedom as little as possible): the coherence of the national tax system,[50] the balanced allocation of tax powers between Member States,[51] the prevention of tax avoidance[52] and the need to ensure the

[45] EEA Agreement.
[46] Court of Justice of the European Union, 6 June 2013, C-383/10, *Commission v. Belgium*.
[47] Court of Justice of the European Union, 23 January 2014, C-296/13, *Commission v. Belgium*.
[48] Court of Justice of the European Union, 28 January 1992, C-204/90, *Bachmann*.
[49] Court of Justice of the European Union, 28 January 1992, C-300/90, *Commission v. Belgium*.
[50] Court of Justice of the European Union, 1 December 2011, C-253/09, *Commission v. Hungary*; Court of Justice of the European Union, 1 December 2011, C-250/08, *Commission v. Belgium*.
[51] Court of Justice of the European Union, 21 February 2013, C-123/11, *A Oy*.
[52] Court of Justice of the European Union, 12 September 2006, C-196/04, *Cadbury Schweppes*.

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effectiveness of tax inspections.[53] The Court can take sanctions against the derogatory measures if they fail to meet the proportionality test.[54]
This general framework should be used as an instrument for dealing with the main questions arising from international taxation.

3.2 Provisions to deal with contemporary cross-border tax problems

International taxation currently has to deal with a series of problems linked to the spread of new technology, changes in the behaviour of all actors in the tax arena (both taxpayers and tax administrations) and diminishing public resources. It is possible to divide these concerns into three categories.

3.2.1 Dealing with tax problems concerning enterprises

Enterprises profit from globalisation and the development of the digital economy by organising their activities in order to pay less tax. The players in the international tax arena, and also States, have identified three contemporary problems that can only be solved by means of international cooperation (which European law, together with the traditional conventional framework, significantly contributes to): transfer pricing, the concept of "permanent establishment" and the concept of "group" with regard to the cross-border compensation of losses.

3.2.2 Dealing with tax problems concerning natural persons

In this connection the political dimension of tax law comes to the fore, embodying the problem of the sovereignty of States, inextricably bound to the relationship between the EU and its citizens/taxpayers. The management of certain situations of double taxation is not ensured by the interaction of bilateral conventions, either because they do not exist or because the High Contracting Parties failed to reach an agreement. As a result, the legal system becomes more complex, not only because it is connected with the situation of individuals, thus entailing public freedoms;

[53] Court of Justice of the European Union, 8 July 1999, C-254/97, *Baxter*; *a contrario*, Court of Justice of the European Union, 17 October 2013, C-181/12, *Yvon Welte*.
[54] Court of Justice of the European Union, 5 July 2012, C-318/10, *SIAT*.

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but also because another international law provision is relevant, i.e. the European Convention on Human Rights.

Overall, there are four critical questions in this domain: the effect of the European Convention on Human Rights, the status of the taxpayer, the regime of social contributions and cross-border withholding tax, and finally the compatibility of exit taxes for individuals.

3.2.3 Dealing with tax problems concerning cooperation between fiscal authorities

This cooperation is governed by two objectives: improving the prevention of non-taxation and organising an assistance procedure for the recovery of taxes. In order to achieve these ends the institutional framework purposes is undergoing a significant evolution.

The traditional institutional framework consists of two levels: conventions generally provide for administrative cooperation for the exchange of information, and assistance procedures for the recovery of taxes.

However, the context has been made more complicated by globalisation. International fraud has called for an adequate response on the part of the tax authorities. Most of them follow the US FATCA provisions, whose entry into force since 1 July 2014 should make it possible to verify its efficiency.

The same goes for the OECD multilateral convention on the automatic exchange of information in tax matters. The final steps in the ratification and adoption process, from 2017 onwards, will provide for the automatic exchange of data which is supposed to verify the level of commitment of States to this project. The evaluation of this operation should take into account the level of creativity employed by taxpayers to avoid its effects.

In a more realistic and probably more efficient way, the results of the work of the EU Directive 2011/16/EU could be evaluated more quickly. Article 288 TFEU makes reference to the flexibility that characterises directives.

With regard to the OECD Base Erosion and Profit Sharing (BEPS) Action Plan in a short-term perspective (due for completion by 31 December 2015), the possibility of a multilateral convention on the existing bilateral conventions represents an innovation the impact of which is likely to be particularly interesting.

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Progress towards a higher degree of fiscal justice at the international level depends on the tension between a European tax law whose evolution is paralysed by the attempts of certain Member States not to give up certain powers, and an international tax regime attracting the unanimous support of the EU countries based on a new version of the international convention.

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