OPINION OF ADVOCATE GENERAL LÉGER
delivered on 22 November 1994 *

1. The four questions referred to the Court for a preliminary ruling by the Bundesfinanzhof in the present case bear an affinity with the series of cases *Commission* v *France* [1] (the 'tax credit' case), *Biehl*, [2] *Bachmann*, [3] *Commission* v *Belgium*, [4] *Commerzbank*, [5] *Halliburton Services* [6] and, above all, *Werner*, [7] the factual and legal aspects of which are very similar. They concern a key question of Community law: what is the impact on domestic income-tax legislation of the Community principle of the free movement of persons as implemented by Article 48 of the EEC Treaty?

2. The relevant tax legislation is as follows.

3. Pursuant to paragraph 1.4 of the Einkommensteuergesetz (German law on income tax, hereinafter 'the EStG'), [8] persons who have no residence in Germany or do not habitually reside there are 'subject to limited taxation' (beschränkt einkommensteuerpflichtig) on the part of their income arising in Germany, whereas residents are subject to 'unlimited taxation'. [9]

4. Those two categories of taxpayers are subject to very different tax regimes.

5. The second are taxed by the German revenue authorities on the totality of their income whilst the first are taxed only on income received within German territory.

6. Applying the principle that the personal and subjective situation of a non-resident — who is therefore subject to limited taxation — will be taken into account by his State of

* Original language: French.

1 — Case 270/83 [1986] ECR 273.

2 — Case C-175/88 [1990] ECR I-1779. Followed by Treaty-infringement proceedings by the Commission against the Grand Duchy of Luxembourg in Case C-151/94, pending.

3 — Case C-204/90 [1992] ECR I-249.

4 — Case C-300/90 [1992] ECR I-305.

5 — Case C-330/91 [1993] ECR I-4017.

6 — Case C-1/93 [1994] ECR I-1137.

7 — Case C-112/91 [1993] ECR I-429.

8 — BGBl I 1987, 657; BStBl I 1987, 274.

9 — Paragraph 1.1, first sentence, of the 1987 EStG.

residence, the German tax regulations withhold from him certain benefits which are available to resident taxpayers: only the latter can benefit from the preferential rates for married couples (the 'splitting tariff'). [10] Certain deductions [11] or reliefs linked, in particular, with their family situation [12] are reduced or eliminated for non-residents. Moreover, the latter are subject to deductions at source from their wages, without any adjustment at the year end. [13]

7. Taxpayers subject to limited taxation are thus taxed objectively, 'as in the case of indirect taxation'. [14]

8. The question of the compatibility of those provisions with Community law has arisen in proceedings brought by a Belgian national, Mr Schumacker, against the Finanzamt Köln-Altstadt.

9. Mr Schumacker has always lived with his family in Belgium. Initially employed in Belgium, he was subsequently employed in the Federal Republic of Germany — from 15 May 1988 to 31 December 1989 — whilst continuing to live in Belgium. [15]

10. The right to impose income tax on Mr Schumacker's wages for that period is vested in the Federal Republic of Germany, the State where he works, under Article 15(1) of the double taxation treaty between Germany and Belgium. [16]

11. Under paragraphs 1.4 and 39d of the 1987 EStG, he is subject to limited taxation and his wages are subject to a deduction calculated in accordance with taxation class I (applicable to German single persons and non-residents, regardless of family status). [17]

12. In response to a complaint from Mr Schumacker, the Finanzamt, by decision of 22 June 1989, refused to calculate the amount

10 — Paragraphs 26 and 26b of the EstG. Under the 'splitting tariff', the overall income of the spouses is aggregated, notionally allocated to each spouse as to 50% and then taxed accordingly. If the income of one of them is high and that of the other low, the splitting evens out the taxable amount and mitigates the progressive effect of the income-tax rates. Without the benefit of splitting, married non-resident employees are subject to the same treatment as single persons.

11 — For example, vocational training expenses (paragraph 33a.2 of the EStG).

12 — Such as the allowance for a dependent child under paragraph 32.6 of the 1987 EStG. See also the fifth sentence of paragraph 50.1 of the 1987 EStG.

13 — Paragraph 42, 42a and 46 of the 1987 EStG.

14 — Paragraph 7 of the Opinion of Advocate General Darmon in *Werner*, cited above. For a detailed examination of the differences between the limited-taxation regime and the unlimited-taxation regime, see the Commission's observations, at I, 3.

15 — His wife received unemployment benefit in Belgium, but only, it seems, for 1988.

16 — Convention of 11 April 1967, based on the OECD model.

17 — If the statement of the plaintiff in the main proceedings is assumed to be correct, under the limited taxation regime he has to pay DM 16 559.64 more than he would have had to pay if he had lived in Germany (plaintiff's observations, part one, at II).

of tax 'on an equitable basis' [18] by reference to taxation class III (applicable to married residents and based on the splitting tariff).

13. The Finanzgericht upheld Mr Schumacker's claim: it ordered the Finanzamt to reassess the tax on his wages for 1988 and to assess that tax for 1989 on the basis of taxation class III.

14. In an appeal on a point of law brought by the tax administration, the Bundesfinanzhof has referred the following questions to the Court of Justice for a preliminary ruling:

'1. Does Article 48 of the EEC Treaty restrict the right of the Federal Republic of Germany to levy income tax on a national of another EEC Member State?

If so:

2. Does Article 48 of the EEC Treaty allow the Federal Republic of Germany to impose a higher level of income tax on a natural person of Belgian nationality, whose sole permanent residence and usual abode is in Belgium and who has acquired his professional qualifications and experience there, than on an otherwise comparable person resident in the Federal Republic of Germany, if the former commences employment in the Federal Republic of Germany without transferring his permanent residence to the Federal Republic of Germany?

3. Does it make any difference if the person of Belgian nationality referred to in question 2 derives almost all (that is 90%) of his income from the Federal Republic of Germany and the said income is also taxable in the Federal Republic of Germany, in accordance with the Double Taxation Agreement between the Federal Republic of Germany and the Kingdom of Belgium?

4. Is it contrary to Article 48 of the EEC Treaty for the Federal Republic of Germany to exclude natural persons who have no permanent residence or usual abode in the Federal Republic of Germany and in that country derive income from employment from the annual wages tax adjustment and also to deny them the possibility of being assessed for income tax with account being taken of earnings from employment?'

18 — Pursuant to paragraph 163 of the 1977 Abgabenordnung.

The first question

15. Can Article 48 of the EEC Treaty restrict the right of a Member State to levy tax on the income of a citizen of another Member State?

16. Noting that direct taxation falls within the exclusive powers of the Member States, the national court expresses doubts as to the possibility of applying Article 48 to national legislation in this sphere. In particular it states that '... nowhere does the EEC Treaty confer express authority to harmonize the direct taxes of the Member States.' [19] In any event, the case-law is not, in its view, sufficiently explicit regarding the existence of a relationship between those provisions. [20]

17. The EEC Treaty contains no provisions similar to those of Article 95 in relation to direct taxation. Article 220 aside, attention has often been drawn to its all but absolute silence in that regard. [21] It is undisputed that the adoption of rules on income tax is a matter left to the Member States. [22]

18. Does this issue thus fall outside the scope of Community law?

19. Let me say first of all that under Article 100 of the EC Treaty, those rules are subject to *harmonization* by unanimous action by the Member States if they have a direct impact on the establishment or functioning of the common market. [23] Taxation is excluded from the scope of Article 100a, which allows harmonizing measures to be adopted by a qualified majority. Unlike VAT, direct taxation is at a purely embryonic stage of harmonization. [24]

20. Secondly, in order to attain the objectives which it sets itself in Article 2 of the EC Treaty, the Community is to establish 'an internal market characterized by the *abolition*, as between Member States, of *obstacles to the free movement* of goods, of *persons*, of services and of capital'. [25]

19 — See the order for reference, at II. B.1.

20 — Ibid.

21 — See Wouters, J., 'The Case-law of the European Court of Justice on Direct Taxes: Variations upon a theme', *Maastricht Journal of European and Comparative Law*, 1994, Vol. 1, No. 2, pp 179 and 180.

22 — See in that connection paragraph 10 of Advocate General Darmon's Opinion in *Biehl*.

23 — Harmonization is compulsory only in the sphere of indirect taxation (Article 99 of the EC Treaty).

24 — See Council Directive 77/799/EEC of 19 December 1977 concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation (OJ 1977 L 336, p. 15), amended by Directive 79/1070/EEC (OJ 1979 L 331, p. 8). See also the Council Directives of 23 July 1990, 90/434/EEC on the common system of taxation applicable to mergers, divisions, transfers of assets and exchanges of shares concerning companies of different Member States (OJ 1990 L 225, p. 1) and 90/435/EEC on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States OJ 1990 L 225, p. 6).

25 — Article 3(c) of the EC Treaty (emphasis added).

21. Thus, even in areas in which they have exclusive powers, the Member States may not adopt measures which, without justification, hamper the free movement of workers (Article 48), members of the professions (Article 52), [26] services (Article 59) or capital (Article 73).

22. The application of those principles is not subject to the precondition of approximation of national laws. As pointed out by Advocate General Mancini in his Opinion in Case 270/83 *Commission* v *France*, [27] 'delay on the part of the Community legislature does not suspend the Member States' obligation to apply their tax laws in a non-discriminatory way'.

23. In that case, the Court upheld the following principle:

'... the fact that the laws of the Member States on corporation tax have not been harmonized cannot justify the difference of treatment in this case' (based on Article 52 of the EEC Treaty). [28]

24. Social security, direct taxation or, for example, the conditions for the award of university diplomas are matters for the Member States. They are nevertheless required to adopt, in those areas, rules which respect the great freedoms laid down by Community law.

25. But it is only to the extent to which such rules have an impact on those freedoms that they come within the scope of Community law.

26. Thus, any tax legislation which introduces discrimination, whether overt or concealed, based on nationality must fall to be examined in the light of Article 48, 52 or 59.

27. More specifically, Article 48(2), by providing for the abolition of all discrimination on grounds of nationality as between workers of the Member States *as regards remuneration*, outlaws any discriminatory tax provision having the effect of undermining the principle of equal treatment in that area. As

26 — See, for example, paragraph 13 of the judgment in Case 154/87 *RSVZ* v *Wolf and Others* [1988] ECR 3897.

27 — End of paragraph 6. On this issue, see the judgment in Case 193/80 *Commission* v *Italy* [1981] ECR 3019, paragraph 17.

28 — Paragraph 24. See also paragraph 11 of the judgment in *Bachmann*: '... such harmonization (of the laws of the Member States) cannot constitute a condition precedent to the application of Article 48 of the Treaty'.

the plaintiff in the main proceedings summarizes the position in his written observations:

'... it is unlawful to convert equal gross wages into unequal net wages by means of higher taxation'. [29]

28. Moreover, Article 7 of Regulation (EEC) No 1612/68 on freedom of movement for workers within the Community[30] requires that all workers who are nationals of a Member State enjoy in the territory of other Member States the same tax benefits as nationals working there. The Council has thus applied the principle of equal treatment to the sphere of taxation.

29. In *Biehl*, the Court held:

'The principle of equal treatment with regard to remuneration would be rendered ineffective if it could be undermined by discriminatory national provisions on income tax'. [31]

30. Clearly, direct taxation, like taxation in other areas within the competence of the Member States, is an area in which the fundamental freedoms laid down in the Treaty must be observed: it is appropriate to cite the Court's words in *Hubbard* [32] in connection with Article 59:

'The effectiveness of Community law cannot vary as between the various areas of national law on which it has an impact.'

31. Finally, the rights granted to Community nationals under Articles 48, 52 and 59 are unconditional. Observance of them cannot depend, in particular, on the content of a double taxation treaty between two Member States. [33]

32. If further evidence were needed of the fact that tax legislation is subject to observance of the great freedoms embodied in the Treaty, Article 73d of the EC Treaty could be cited. Article 73b having laid down the principle that all restrictions on capital movements between Member States and between Member States and non-member countries is prohibited, Article 73d provides that the Member States are entitled 'to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in

29 — Page 24.

30 — Council Regulation of 15 October 1968, OJ, English Special Edition 1968 (II), p. 475.

31 — Paragraph 12.

32 — Case C-20/92 [1993] ECR 1-3777, paragraph 19.

33 — See paragraph 26 of the judgment in Case 270/83 *Commission* v *France*, cited above.

the same situation with regard to the place where their capital is invested', going on to say, in paragraph 3, that such measures 'shall not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments ...'.

The second question

33. A preliminary observation is called for: it is true that, by contrast with *Werner*, this case certainly comes within the scope of Community law. A German national working in the Federal Republic of Germany where he acquired his professional qualifications, Mr Werner never exercised the freedoms conferred by the Treaty, particularly that of establishing himself *in another Member State*. The only foreign element was the fact that he resided in the Netherlands. In this case, Mr Schumacker, a Belgian national who acquired his qualifications and professional experience elsewhere than in the Federal Republic of Germany, [34] exercised the right of freedom of movement for workers laid down in Article 48 of the Treaty in order to go to Germany and take up employment there. The situation is therefore not purely internal to a Member State. [35]

34. That point having been clarified, I shall reformulate the second question in the following terms:

'May the tax legislation of a Member State, without infringing Article 48 of the Treaty, tax a non-resident employed in that State more heavily on his income than a resident in the same employment?'

35. The criterion of residence is the main pillar of international tax law. Chosen by almost every State in the world, it is given precedence over nationality 'which involves taxation by a State of persons who may have lost all links, in particular those of an economic nature, with that State'. [36]

36. The logic of the distinction between residents and non-residents is clear: by choosing to reside in a particular State, a person assumes the obligation to contribute to the costs of public administration and the public services made available to him by that State. It is therefore logical that that State should tax the entirety of his income, on a comprehensive basis. It is also that State, where the taxpayer has focused his family life, which will grant him allowances and reliefs. There

34 — See the Order from the national court.

35 — It cannot of course be contended that freedom of movement for workers applies only where a worker has transferred his residence to his State of employment. See Article 1 of Council Regulation No 1612/68.

36 — Opinion of Advocate General Darmon in *Commerzbank*, cited above, paragraph 37.

is a personal link between the taxpayer and his State of residence.

37. Conversely, the State of employment taxes the non-resident in a quasi objective manner only on his income arising in its territory. The taxpayer, indeed, has no other link with that State than the economic activity which he carries on there.

38. Thus, clearly, tax law draws a distinction between residents and non-residents because they are not, objectively, in the same situation. That distinction, moreover, is to be found at the heart of the OECD model double taxation convention on income and capital. [37]

39. Application of the principle of non-discrimination to the sphere of taxation calls for great circumspection. As has been observed,

'To anyone who is somewhat familiar with tax law, it is clear that the concept of de facto non-discrimination could very easily result in the *disintegration* of national tax systems. Even were the Court to limit itself to the elimination of the differences in tax treatment between taxpayers based on nationality or on residence, the resulting *chaos* in income tax would be considerable'. [38]

40. In order to guarantee freedom of movement for workers within the Community, Article 48(2) prohibits all discrimination on grounds of nationality between workers of Member States regarding, in particular, remuneration.

41. Citing *Sotgiu*, [39] the Court held in *Biehl*

'...the rules regarding equality of treatment forbid not only overt discrimination by reason of nationality but also all covert forms of discrimination which, by the application of other criteria of differentiation, lead to the same results'. [40]

42. The Court has recognized that a distinction based on residence, although applicable without distinction to nationals and non-nationals, should be viewed in the same way

37 — See in particular Article 4(1) of the model convention of September 1992.

38 — Vanistendael, F.: 'The Limits to the New Community Tax Order', *CML Rev.*, 1994, p. 293 (emphasis added).

39 — Case 152/73 [1974] ECR 153, paragraph 11.

40 — Paragraph 13. See also, with regard to Article 52, paragraph 14 of the judgment in *Commerzbank* and paragraph 15 in *Halliburton Services*.

as a distinction based on nationality where the non-residents are in the main non-nationals. [41]

43. The Court concluded from this that Article 48 precludes legislation which deprives a taxpayer who is a resident for only part of the year of the right to reclaim overpayments of tax where permanent residents are entitled to such repayment. [42]

44. However, the possibility cannot be excluded 'that a distinction based on the ... place of residence of a natural person may, under certain conditions, be justified in an area such as tax law'. [43]

45. A tax provision based on the criterion of residence and having discriminatory effects does not encroach upon the principle of freedom of movement for workers provided that it pursues an objective in the public interest (such as upholding the coherence of the national tax system) and is strictly necessary in order to achieve that aim. In its judgment in *Commission* v *Belgium*, [44] the Court recognized that a tax provision restricting the free movement of workers did not infringe Article 48 of the Treaty provided that it was justified 'by the need to safeguard the cohesion of the tax system at issue'. [45]

46. Under Belgian tax law, contributions in respect of supplementary old-age or death insurance are deductible from taxable income only if they are paid to companies established in Belgium or to the Belgian establishment of a foreign insurance undertaking. The Court held that the cohesion of the tax system (namely the link between deductibility of contributions and the subsequent taxation of the income or capital paid out by the insurance company) could not be ensured by less restrictive measures and that the tax provision in question was therefore compatible with Article 48 of the Treaty.

47. Since the judgments in *Bachmann* and *Commission* v *Belgium*, the Court has held that national rules which are discriminatory within the meaning of Article 48(2) may, despite such discrimination, be justified for overriding reasons of public interest. The exceptions to the principle of non-discrimination laid down by that article are not merely those referred to in paragraphs 3 and 4 thereof.

41 — Paragraph 14. See also paragraph 9 of *Bachmann* and paragraph 15 of *Commerzbank*.

42 — Paragraph 19.

43 — Paragraph 19 of the judgment in Case 270/83 *Commission* v *France*, cited above.

44 — Cited above, footnote 4.

45 — Paragraph 21.

48. The Court thus applies the 'rule of reason' to discriminatory tax rules intended to temper the effects of bringing within the scope of Articles 48 and 52 national rules which apply without distinction and prevent or hamper the free movement of workers. [46]

49. Those are the principles which, I suggest, should be applied in the present case.

50. Is there discrimination in this case? If so, is it justified?

51. It can be conceded that the majority of non-residents are non-nationals [47] and that a benefit reserved exclusively for residents conceals discrimination based on nationality.

52. But it is also necessary, at the very outset, for there to be a clear indication of discrimination.

53. As we know, 'discrimination consists solely in the application of different rules to comparable situations or in the application of the same rule to differing situations'. [48]

54. In tax matters, the Court takes particular care to ensure that the existence of discrimination is actually established.

55. Thus, in its judgment in Case 270/83 *Commission* v *France*, cited above, the Court held that, where companies having their registered office in France and branches and agencies situated in France of companies having their registered offices abroad are subject *to the same tax regime* and no distinction is drawn for the purpose of 'determining the income liable to corporation tax', they may not be *treated differently* as regards the grant of an advantage related to taxation, such as tax credits. [49] Similarly, in *Biehl*, the taxable amount over the period concerned was the same for residents and non-residents. Finally, in *Commerzbank*, resident companies enjoyed tax benefits

46 — See the judgment of 31 March 1993 in Case C-19/92 *Kraus* [1993] ECR I-1663. See, on this point, with respect to the *Bachmann* judgment, Vanistendael, F., 'The Limits to the New Community Tax Order', cited above, p. 312: 'The non-discrimination rule ... has the following meaning: even though any *de facto* discrimination is in principle to be considered as a violation of the basic freedoms in the Treaty, some rules resulting in *de facto* distinction or discrimination can be justified by general interest or policy objectives, provided those rules make distinctions on the basis of criteria that are objective and directly necessary to achieve the policy goals'.

47 — See the judgments cited above: *Biehl*, paragraph 14, *Bachmann*, paragraph 9, *Commission* v *Belgium*, paragraph 7, and *Commerzbank*, paragraph 15.

48 — Judgment in Case 283/83 *Racke* v *Hauptzollamt Mainz* [1984] ECR 3791, paragraph 7.

49 — Paragraphs 19 and 20.

which were not available to non-residents *in the same tax situation.*

56. It is therefore necessary to verify in this case whether 'similar situations' are 'treated differently'. [50]

57. Having regard to the procedures and conditions for the taxation of income, is there an objective difference of circumstances which could justify different treatment? [51]

58. The *ratio legis* of the German tax rules is clear: those in the category of taxpayers 'subject to unlimited taxation', which includes residents, are taxed on worldwide income. [52] Enjoying as they do the benefits provided by their State of residence, they must contribute through taxation to the expenditure thereby incurred. Moreover, it is that State which is best placed to know-or find out-what their personal circumstances are and to tax them individually by granting various allowances or reliefs for family responsibilities or business expenses (Werbungskosten), and so forth. That is the centre of the taxpayer's essential interests. [53]

59. On the other hand, a person 'subject to limited taxation' (here, a non-resident) is taxed in the Federal Republic of Germany only on the part of his income arising there. He is taxed objectively, regardless of his personal circumstances, according to the principle that those circumstances will be taken into account by the tax administration in his State of residence, which knows him better, in accordance with the rules of international tax law. [54] As the national court observed, 'It is thus not the taxpayer personally who is linked with the national territory, but the work done by him'. [55]

60. The taxpayer's personal situation is therefore taken into account only in his State of residence, where the taxation takes account of all his income [56] in order to avoid duplication of the personal reliefs and deductions granted to him.

50 — Judgment in Case 810/79 *Überschär* [1980] ECR 2747, paragraph 16.

51 — See the final sentence of paragraph 20 of Case 270/83 *Commission* v *France*, cited above.

52 — The taxable amount is reduced to the amount of income arising in the State of employment, in order to avoid double taxation.

53 — The taxpayer is subject to tax in his State of residence simply because he 'lives' on the territory of that State. See the Order for reference, II, B, 2.1.

54 — Article 24 of the OECD 1977 Model Tax Convention: 'This provision shall not be construed as obliging a Contracting State to grant to residents of the other Contracting State any personal allowances, reliefs and reductions for tax purposes on account of civil status or family responsibilities which it grants to its own residents.'

55 — Order from the national court, II, B, 2.1.

56 — Paragraph 1(1) of the 1987 EStG.

61. It is only in his State of residence that the 'splitting' approach can be used, which presupposes that all the income obtained by both spouses, both at home and abroad, is taken into account.

62. It is a cohesive system: if the Federal Republic of Germany took account of the personal circumstances of a taxpayer subject to limited taxation — which it could do only in respect of the income earned there — those circumstances would be taken into account twice, by the State of employment and by the State of residence, leading to an unjustified tax benefit. The different systems to which residents and non-residents are subject make it possible to *avoid duplication of benefits.* That is why, under Article 24(3) of the OECD model convention on double taxation, a contracting State is not obliged to grant residents of another contracting State the personal deductions, reliefs and rebates which it grants its own residents. [57]

63. There is thus no discrimination between a person subject to unlimited taxation and one subject to limited taxation because *they are not in comparable circumstances.* Taxation of the former's worldwide income cannot be compared to the taxation of the latter, which is limited to the income received in the State of employment. Different situations are treated differently. The abovementioned Article 24 of the OECD Model Convention is very clear in that respect: residents and non-residents are not in the same situation and a distinction may be drawn between them with regard to taxation without the latter having any right to invoke the principle of non-discrimination.

64. It cannot therefore be contended that a non-resident subject to limited taxation is, in principle, taxed 'more heavily' than a resident subject to unlimited taxation. [58] The basis of taxation is not the same [59] and the individual circumstances of the person concerned may be taken into account under very favourable conditions by his State of residence.

65. But does this system not display a weakness where the non-resident taxpayer receives all (or almost all) his income in his State of employment and, under the double taxation treaty between the State of residence and the State of employment, such income is

57 — See paragraph 22 of the commentary on the second sentence of Article 24(3) of the OECD Model Double Taxation Convention. The Greek Government emphasizes correctly that the Court must not allow 'the residents of any Community country who earn wages in more than one country to have the benefit, on more than one occasion, of reliefs or deductions in respect of tax on income, since they would be entitled to ask for such reductions or reliefs to be granted to them in all those countries where they earned income which was taxable in the country where that income arose' (observations, p. 8).

58 — That view is expressed at p. 7 of the French Government's observations.

59 — Income received abroad is not included in the taxable amount to which progressive tax rates are applied in the State of employment, which may constitute a considerable advantage.

taxable only in the latter State? That is the specific issue raised in the third question.

The third question

66. Not being subject to taxation in his State of residence, where he does not receive sufficient income, a taxpayer in the circumstances of the plaintiff in the main proceedings [60] — he is subject to limited taxation in his State of employment — will not have his personal circumstances taken into account in any State: the State of residence does not tax him at all and his State of employment regards him as subject to limited taxation and disregards his personal circumstances.

67. This sort of 'negative conflict' of jurisdiction between the State of employment and the State of residence (which both refuse to grant tax relief in respect of personal and family responsibilities) leads to 'overtaxation' of non-residents. Does this constitute discrimination?

68. The practical importance of the question should be emphasized: frontier workers — in very many cases — receive all their income in the State where they are employed. They are therefore, in that respect, in a situation wholly comparable with that of residents. Can the distinction between residents and non-residents be invoked against them when, objectively, they are for tax purposes *in the same situation as residents*?

69. That situation is reminiscent of the *Biehl* case, in which the Court emphasized that breach of the principle of equal treatment was particularly clear where the non-resident taxpayer *received income only in the Grand Duchy of Luxembourg.* [61]

70. A national of a Member State who exercises his right of freedom of movement under Article 48, to work in another Member State (where he receives all his income) whilst continuing to reside in his State of origin, will have to pay tax on the income received in his State of employment without his personal circumstances and his family responsibilities being taken into consideration.

71. This leads to clear discrimination at the expense of the non-resident, who is subject to a different tax regime from that applicable to residents, where 'the income liable to ...

60 — It seems that the Kingdom of Belgium ceased paying unemployment benefits to Mr Schumacker's wife in 1988. Mr Schumacker receives income in his own right only in the Federal Republic of Germany.

61 — Paragraph 16 of the judgment. See also paragraph 10 of the Opinion of the Advocate General in that case: 'The manifestly discriminatory nature of the rule at issue is evident in particular in all cases in which the national concerned received no income during the year in question in the Member State of origin or destination'.

tax' is determined in the same way [62] and both are in the same specific situation from the tax point of view.

72. More particularly, the non-resident is refused the benefit of 'splitting', the effect of which is to moderate the progressive nature of the tax rates.

73. The consequences of such discrimination for the free movement of persons has not escaped the Commission, which on 21 December 1993 adopted a recommendation (97/79/EC) on the taxation of certain items of income received by non-residents in a Member State other than that in which they are resident: [63]

'the free movement of persons may be impeded by personal income tax arrangements which have the effect of imposing a heavier tax burden on non-residents than on residents *in comparable situations*'. [64] The former must not, '*where the preponderant part of their income* is received in the country of activity, be deprived of the tax reliefs and deductions enjoyed by residents'. [65]

74. Consequently, the Commission recommends that the Member States do not subject the income of non-residents received in the State of employment to higher taxation than that State would impose if the taxpayer and his wife and children resided there, provided that such income constitutes at least 75% of his total taxable income. [66]

75. The existence of discrimination is not in doubt where the non-resident receives all his income in his State of employment. What is the position where he receives most or almost all his income in the latter State? At what point must he be treated as if he were a resident? In its recommendation, the Commission puts the threshold at 75%. The German and Netherlands rules put it at 90%.

76. I consider that, in the absence of such rules, only an appraisal of the facts — falling to the national court — will make it possible to determine the threshold as from which the income in the State of residence is *sufficient* for the personal circumstances of the person concerned to be taken into account by the tax authorities of that State. Only the residents of that State who have not reached that threshold can be placed on the same footing as residents of the State of employment where they receive the major part of their income.

62 — Paragraph 19 of the judgment in Case 270/83 *Commission* v *France*, cited above.

63 — OJ 1994 L 39, p. 22.

64 — Second recital, emphasis added.

65 — Sixth recital, emphasis added.

66 — Article 2(1) and (2).

77. What justification might 'save' the German rules in the light of Article 48 of the Treaty?

78. Where one encounters discriminatory tax rules, one examines very rigorously any grounds for justification. Thus, a tax disadvantage is not necessarily justified by the fact that it may be balanced out by an advantage. [67]

79. Two justifications have been put forward in this case.

(a) *The personal situation of a taxpayer must be considered only by the tax administration in the State of residence, which alone is capable of ascertaining it precisely.*

80. In that connection, the exchange of information between national administrations has expanded, particularly by virtue of Directive 77/799 [68] (even if cooperation between tax administrations in the Member State is limited by Article 8(1) of that directive), [69] and Directives 79/1070/EEC [70] and 91/12/EEC [71] which amended it.

81. Relying on those directives, the Court rejected the argument that it was difficult for a tax administration to gather the information necessary for the taxation of a person established in another Member State. [72]

82. Even if it were assumed that such cooperation is still regarded as insufficient today, I consider that the reasoning adopted by the Court regarding the deductibility of insurance contributions can be transposed to the deductions or reliefs which a person subject to unlimited taxation may claim:

'However, the inability to request such collaboration (between tax authorities of Member States) cannot justify the non-deductibility of insurance contributions. *There is nothing to prevent the tax authorities concerned from demanding from the person involved such proof as they consider nec-*

67 — See paragraph 21 of the judgment in Case 270/83 *Commission* v *France*, cited above.

68 — Cited above, note 24.

69 — See paragraph 20 of *Bachmann*.

70 — Council Directive of 6 December 1979 amending Directive 77/799/EEC concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation (OJ 1979 L 331, p.8).

71 — Council Directive of 25 February 1992 on the general arrangements for products subject to excise duty and on the holding, movement and monitoring of such products (OJ 1992 L 76, p. 1).

72 — Paragraph 18 of *Bachmann* and paragraph 22 of *Halliburton Services*.

essary and, where appropriate, from refusing to allow deduction where such proof is not forthcoming'. [73]

(b) *The cohesion of the tax system precludes treating non-residents in the same way as residents in such circumstances*

83. I have shown that the distinction between residents and non-residents is understandable where the latter's income arises both in the State of residence and in the State of employment. On the other hand, the tax status of a non-resident must be eligible for the same treatment as that of resident where he receives his income under exactly the same conditions as a resident. Moreover, overtaxation of the non-resident is, in such circumstances, particularly unfair since it has the effect of increasing his tax payment in a State where he does not reside.

84. That being so obviously the case, the Federal Republic of Germany initially adjusted its tax rules so as to bring frontier workers from the Netherlands who received at least 90% of their worldwide income in Germany within the tax regime applicable to German residents, [74] in particular the benefit of 'splitting'. Subsequently, the German legislature brought the treatment of all non-residents receiving at least 90% of their overall income in Germany into line with that of residents of that State, apart from the benefit of 'splitting'. [75]

85. To justify the different treatment under its rules for frontier workers from Belgium as compared with those from the Netherlands, the German government contends that to extend to the former the status of taxpayer subject to unlimited taxation would expose it to the risk of having to accord that status generally to all non-resident or non-national workers, who could invoke the constitutional principle of equal treatment.

86. Let me say straight away that unequal treatment already exists, and was even ascer-

73 — Paragraph 20 of *Bachmann*, emphasis added.

74 — Law of 21 October 1980 on the implementation of the Additional Protocol of 13 March 1980 to the Convention of 16 June 1959 between the Federal Republic of Germany and the Kingdom of the Netherlands (AGGrenzg NL, BGBl I 1980, 1999, BStBl I 1980, 725). It should also be noted that, reciprocally, Netherlands tax law treats in the same way as persons subject to unlimited taxation those who receive at least 90% of their worldwide income in the Netherlands but do not reside there ('Resolutie' of the Secretary of State for Finance of 21 December 1976, No 27-621 782, and of 28 December 1989, No DB 89/2184, BNB 1990/100 and, since 1 January 1990, Wet op de Inkomstenbelasting 1964, Articles 53a and 53b). See also paragraph 11.5 of the Commission's observations.

75 — Gesetz zur einkommensteuerlichen Entlastung von Grenzpendlern und anderen beschränkt steuerpflichtigen natürlich Personen und zur Änderung anderer gesetzlicher Vorschriften (Grenzpendlergesetz) of 24 June 1994, BGBl, I No 39, p. 1395.

tained by the Bundesfinanzhof in a judgment of 20 April 1988: [76]

'It would be contrary to paragraph 3 of the Basic Law to treat frontier workers from other neighbouring States differently from those from the Netherlands'.

87. In any event, the German government cannot justify an infringement of Article 48 by pleading the excessive financial consequences of making generally available a right which it has already granted to certain non-residents. The Court has already responded to an argument of that kind in its judgment in Case 270/83 *Commission* v *France*. [77] Whilst a Member State may limit entitlement to a tax benefit, it may only do so if it observes the principle of non-discrimination.

88. In any event, it is evident from recent German tax legislation that the assimilation, in certain specific circumstances, of non-residents to residents does not endanger the cohesion of the national tax system. On the contrary, it enables the principle of equal treatment to be upheld.

89. What is the position regarding 'splitting', of which the benefit is withheld from non-residents by the Grenzpendlergesetz?

90. There is no risk in this case of the taxpayer's personal circumstances being taken into account twice, because he is not taxed in his State of residence.

91. The difficulty arises from the fact that, in the present case, application of the 'splitting tariff' means that the income received by the spouse in the State of residence (unemployment benefits), which is not taxable in Germany, is taken into account.

92. The national court concedes that 'taking account thereof for the purposes of progressive tax rates ... appears technically feasible', [78] which is confirmed by the fact that frontier workers from the Netherlands already enjoy that benefit.

93. I agree that it would be impossible to extend 'splitting' to non-residents if it were established that residents in Germany, in circumstances comparable to those of the plaintiff in the main proceedings, were deprived of it.

76 — I R 219/82, BStBl 1990, Teil II, p. 701, BFHE Bd 154, p. 38, 46.

77 — Paragraph 25.

78 — Paragraph II, B, 2.2 of the Order.

94. However, spouses residing together in Germany are subject to unlimited taxation and 'splitting' is systematically available to them. Moreover, it is apparent from the findings of the national court that a married couple residing at the same time in both Germany and Belgium could also qualify for it. [79]

95. I conclude from this that, for application of the tax by progressive rates, the income of a spouse, whether or not resident, may be taken into consideration. [80]

96. Finally, the benefit of 'splitting' cannot be withheld because of difficulties in exchanging information between national tax administrations. I have already considered this point. [81]

97. *In the extremely specific case referred to the Court, the cohesion of the tax system does not require a distinction between residents and non-residents but, on the contrary, requires the latter to be treated in the same way as the former.* Being subject to the same tax obligations, they must enjoy the same benefits and, in particular, the same tax reliefs.

98. Let me emphasize, in conclusion, that the distinction between residents and non-residents is not absolute. The tax rules of several Member States deem certain persons who do not live there to be residents and subject them to unlimited taxation. Paragraph 1(2) of the EStG, which is concerned with non-resident civil servants, or the German tax regime for people with dual residence are two examples of this.

The fourth question

99. Does Article 48 require the State of employment to apply to non-residents in the circumstances of the plaintiff in the main proceedings the principle of annual adjustment of deductions at source in respect of wages tax (Lohnsteuerjahresausgleich) and assessment of income tax by the administration (Veranlagung zur Einkommensteuer)? In other words, does Article 48 require equal treatment regarding not only substantive tax rules but also at procedural level?

100. The German rules provide for annual adjustment of deductions at source in respect of wages tax paid by persons subject to unlimited taxation. The employer is required to refund part of the income tax to the employee where the total amount retained monthly exceeds the amount resulting from the tax scale for the year. Non-residents —

79 — Ibid.

80 — See the observations of the plaintiff in the main proceedings, pp. 43 and 44. See also Saß, G., 'Zum Einfluß der Rechtsprechung des EuGH auf die beschränkte Einkommen- und Körperschaftsteuerpflicht', *DB*, Heft 17, of 24 April 1992, p. 857, at 862.

81 — See paragraph 80 et seq.

who are subject to limited taxation — do not qualify for any such adjustment: [82] the sum of the monthly deductions at source constitutes the definitive taxation.

101. Whilst the non-resident may thus be able to avoid possible retroactive taxation, [83] the important point is that he is deprived of the possibility of claiming for exceptional expenditure or extraordinary financial burdens which might give rise to a tax refund. He is placed at a particular disadvantage if he leaves his State of employment *in the course of a year* (or if he takes up work there during the course of a year, as in the case of the plaintiff in the main proceedings in 1988).

102. Provided that the non-resident's situation is *comparable* to that of the resident, in other words he receives all or almost all his income in the State of his employment, is such a difference of treatment compatible with Article 48 of the Treaty?

103. That question was, in my view, settled by the judgment in *Biehl*.

104. In that case, a taxpayer who left the Grand Duchy of Luxembourg during a year was unable, unlike residents, to receive a refund at the year end of any overpayment received by the tax administration as a result of deductions at source. Finding that taxpayers who leave their State of employment (or establish themselves there) during the course of a year are mainly nationals of other Member States, the Court identified disguised discrimination. [84]

105. In the present case, by depriving non-residents of the right to annual adjustment of deductions at source, the German tax rules deprive them of a *benefit*, namely the right to the refund of any overpayment (where the monthly deductions exceed the total amount of tax due for the year in question), which, by contrast, residents may claim.

106. The obligation to grant the nationals of another Member State the same tax benefit as nationals extends to procedural rules and arrangements for recovering tax. The Court has already taken the view that the mere possibility of an administrative appeal against a tax decision which is considered unfair could not justify maintaining a discriminatory procedural tax provision. [85]

82 — Paragraph 50.5 of the EStG.

83 — See the Order from the national court, II, B, 4.

84 — Judgment in *Biehl*, paragraph 14.

85 — Ibid., paragraphs 17 and 18.

107. Consequently, it seems to me that there is a breach of Article 48 of the Treaty which, moreover, the Commission identified in a written reply to a question from a Member of the European Parliament on 26 October 1992. [86]

108. Two last remarks are called for.

109. First, the solution which I advocate is compatible with the Court's judgment in *Werner* which, it will be remembered, concerned a situation internal to a Member State in which the Court perceived neither disguised discrimination on grounds of nationality nor an infringement of Article 52.

110. Secondly, there is no risk here that, after a round of fiscal forum shopping, the taxpayer would choose to establish his residence in the State where taxation is most favourable, as the Danish government fears. To align the tax regime of non-residents with that of residents where both receive all their income in the Member State of employment has the effect, on the contrary, of rendering the choice of residence *neutral* from the tax point of view.

111. I therefore suggest that the Court rule as follows:

'(1) Tax rules which apply to residents and non-residents different conditions regarding income tax may fall within the scope of Article 48 of the EC Treaty.

(2) In principle, that article does not preclude a non-resident employed person from being taxed by the State of employment more heavily than a resident in the same employment where they are not in comparable situations from the tax point of view.

(3) On the other hand, that article prohibits a Member State A from fixing, in the case of a worker residing within the territory of a Member State B, who is in

86 — Question No 2579/91 (OJ 1993 C 16, p. 1).

employment within the territory of Member State A and (1) receives in Member State A all or most of his income and (2) does not receive in Member State B sufficient income to be taxed individually on the basis of his personal circumstances, income tax at a level higher than that payable by a person residing in Member State A who is assessed on the same taxable amount. Such a worker must therefore be entitled to the benefit of the same tax benefits as a resident.

(4) Under Article 48, an employed person may not be deprived of the annual adjustment of deductions at source in respect of income tax and assessment to wages tax by the administration if those benefits are available to a resident employed person in the same situation'.