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Editorial

Tax coordination: a joint responsibility of the Member States. Still a fantasy?

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Removal of the tax obstacles within the EU by means of harmonization continues to be a difficult course to take. For direct taxation, the European Commission has now opted for a practical solution. 'Coordination' is now the magic word. In the Communication 'Coordinating Member States' direct tax systems in the Internal Market' of 19 December 2006, the Commission called for a coherent and coordinated treatment which, amongst other things, implies that an end is to be made to discrimination and double taxation and unintended non-taxation and abuse will be avoided. The Member States must exert themselves in order to ensure that the existing national tax systems can be made 'to work seamlessly together'. In two other Communications on exit taxation, and the tax treatment of losses, the Commission indicated how it viewed such a coordinated approach in these areas. More Communications on other problem areas are to follow in the future.

The initiative of the Commission to have the national tax systems dovetail more with each other must be applauded. But what if the Member States do not make the moves? The Member States are already in the process of concluding bilateral tax treaties in order to resolve part of the problems outlined by the Commission (particularly juridical double taxation and abuse). The Commission does not really have a means of enforcement to admonish the Member States to proceed to coordination. In the *Kerckhaert* case, for example, the ECJ ruled that juridical double taxation as such was not a forbidden restriction of the EC Treaty freedoms but a 'result from the exercise in parallel by two Member States of their fiscal sovereignty'. It is thus not a simple matter to point at which Member State is 'guilty'. The double taxation exists because two sovereign states exercise their right to levy tax and they have not coordinated this with each other. There is no question of a restriction forbidden by the EC Treaty freedoms, but of what we can term a 'disparity', or a 'distortion', or in the words of Advocate-General Geelgoed, a 'quasi-restriction'. Such disparity must be resolved by harmonization or – exactly yes, by coordination – of the national systems. In *Kerckhaert,* the ECJ also noted: 'Consequently, it is for the Member States to take the measures necessary to prevent situations such as that at issue in the main proceedings by applying, in particular, the apportionment criteria followed in international tax practice'.

This coordination must proceed voluntarily, by having the Member States' tax treaties function properly. Or perhaps not: in *Kerckhaert,* the ECJ noted that the removal of juridical double taxation was 'essentially' the purpose of the tax treaty concluded between Belgium and France. To subsequently remark: 'However, that convention is not at issue in the preliminary reference at hand'. But what does the ECJ mean with this? In fact, the ECJ found that the object of the tax treaty was to remove double taxation and failed, but the question of whether the applicability of the tax treaty could be in conflict with the Treaty freedoms had not been put before them. Could this mean that the ECJ is leaving the option open for the opinion that that *if* a treaty is concluded, this must achieve the object for which it was drawn up (in this case, the avoidance of double taxation)? Or am I reading too much into the remarks of the ECJ? I am not sure. What is striking is that after the *Kerckhaert* judgment, the European Commission simply continued its infringement proceedings against Belgium on exactly the same issue. Could it be so that the Commission still sees an opportunity?

Well, there certainly is one: as said, from *Kerckhaert* it can be derived that a Member State does not have to grant prevention of juridical double taxation. In the *De Groot* case of 2002 there was a question of juridical double taxation, the Netherlands did provide for prevention in that case on the basis of the applicable tax treaty, however, according to the ECJ, the Netherlands did *not* provide for *sufficient* prevention. But if you are not obliged to provide for any prevention of juridical double taxation how can the same EC law be triggered if you provide for *insufficient* prevention of double taxation? Is that because the *De Groot* case concerned the prevention such as was imposed in the tax treaty? In other words: in itself, a Member State does not have to provide for prevention of juridical double taxation, but *if* it does (in a tax treaty) then it must duly observe EC law. Is that how the ECJ mind works?

Of further importance is that in the European lobbies, debate has been in progress as to whether the

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European Commission could not address two Member States *at the same time* as to their responsibility to, for example, resolve double taxation. Article 293 of the EC Treaty lays down that the Member States, in so far as is necessary, should enter into negotiations on the abolition of double taxation within the Community. In the past, the ECJ had ruled that this provision was not of direct effect, but has it not eventually become time to remind the Member States of their responsibility, after 50 years, to conclude tax treaties and subsequently duly to comply with them? The problem with the avoidance of double taxation is that it is not up to the ECJ to decide *which* Member State should avoid double taxation. The ECJ would then be regulating the taxation powers between the Member States, and this is something that the Member States themselves must do. However, *if* two Member States conclude a tax treaty and divide the taxation powers, could the European Commission not point out to the Member States that they must do all in their power to respect the division of the taxations powers? Thus, grant prevention of double taxation if such is prescribed in the tax treaty, no *treaty override*, and enter into consultation with the other Member State in the event of differences in interpretation of the tax treaty? And can the ECJ not confirm that the Member States must strive to follow the object of the tax treaty and to exert themselves to that effect within a certain period to achieve this? And if Member States cannot demonstrate sufficient exertion to remove double taxation: impose a penalty. On both.

If the ECJ should revert to this course, the ECJ would respect the fact that it was up to the Member States to divide the taxation powers between each other on the one hand, but that it did attach consequences if such a division has been established on the other. In my view, in an internal market (which is what we wanted is it not?) that would be no more than normal.

Is the above simply fantasy? As said, there is ongoing heated speculation and debate on such possibility in the European lobbies. In November 2006, Advocate-General Kokott put forward this question during the FIDE World Congress in Cyprus.[1] The debate is often fuelled by Volker Heydt, who works with the European Commission as head of the department of 'control of the application of EU legislation and state aid/direct taxation'. This year, in April, Volker Heydt publicly voiced his (personal) views during the Confédération Fiscale Européenne (CFE) forum in Brussels. It is not yet the situation that in tax matters, the European Commission actually reminds two Member States of their joint responsibility to prevent double taxation. It is also not so that there are no catches to this concept. I must also give it further deliberation. Nevertheless, this is a refreshing new debate which deserves further attention and research in literature. This opinion thus serves as a modest step in that direction.

[1] *See*: Federation Internationale de Droit Europeene (FIDE) 2006, Direct tax rules and the EU fundamental freedoms: origin and scope of the problem; National and Community responses and solutions (topic 1), General reporter, Paul Farmer; Community reporter, Dennis Weber, ISBN 9963-9320-0-2.