Editorial

Using the Treaty of Maastricht to combat Discriminatory Tax Practices in 1995. Examples in France

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The underlying purpose of tax treaty non-discrimination clauses is to abolish unfair treatment based on nationality. Such clauses are founded on the clearly defined principle of the free movement of persons, services and capital according to the Treaties of first Rome and now Maastricht (Articles 7, 52 and 95), and usually developed along the lines of the OECD model treaty recommendations.

Let us refer in this instance to Article 24 of the OECD Commentary concerning non-discrimination, whereby:

> '... nationals of a Contracting State *may not be subjected* in the other Contracting State *to any taxation* of any requirement connected therewith which is *other or more burdensome than the taxation* and connected requirements to which nationals of the other Contracting State in the same circumstances are or may be subjected... '.

These provisions aim to clearly define the concepts of nationality and residence as far as private individuals are concerned, unlike French case law which only recently clarified the problem of discrimination where legal entities are concerned opting in favour of the distinction based on corporate seat.

At the level of the European Court of Justice, case law reflects a concern with equal treatment being strengthened not only through prohibiting discrimination based on corporate seat or nationality but also through combating any hidden forms of *de facto* discrimination due to the application of different criteria at State levels.

Despite EC Treaties, OECD Fiscal Affairs Committee and the European Court of Justice commitment to legitimating the principle of non-discrimination at the European level, national authorities have failed to fully eliminate search practices. Indeed, we shall see how in certain instances discrimination is inherent in the very drafting of national legislation.

In France, although case law questions the discrimination existing between residents and non-residents, actual practice continues to reflect the gap between European principles and national realities. This fact is illustrated by an abundance of examples. However, they can be considered in the positive light of opportunities for action.

Heightened awareness of areas of discrimination represent so many occasions for action at the level of judicial and administrative negotiation and even litigation with the goal of promoting harmonization of national positions with EC directives.

1. Inherent Discrimination

French Tax Code (hereafter CGI) Article 212 sets forth the principle of deductibility of shareholder loan interest and limits the amount to one and a half times the capital of the borrowing company where the lender, partner or shareholder is in *de facto* or *de jure* control of the company.

According to the terms of CGI Article 145, such interest can escape the abovementioned limitation when a parent company is lending to its subsidiary. This implies that said parent company be of French nationality. The compatibility of this domestic provision with treaty directives according to OECD Model Treaty Guidelines and Maastricht Treaty is questionable.

2. Insidious Discrimination

CGI Article 150C provides exemption of capital gains realized on principal residence for French nationals. It further stipulates that the exemption in question can also benefit buildings representing residence in France of French residents who are nationals of other countries providing the transferor has been fiscally domiciled in France on an on-going basis for at least one year prior to the transfer and that such transferor has enjoyed free disposal of the property since its acquisition for at least three years.

Since it will clearly be more difficult for a foreign national to fulfil such criteria, the very terms of the provision breed discrimination, without there having necessarily been any intent to this effect.

3. Deliberate Discrimination

French branches of foreign companies suffer double taxation on their profits: once at the level of corporate income tax and again with the withholding levied on profits deemed distributed to their foreign sitused head office (CGI Article 115).

In certain circumstances, the foreign company can obtain a refund of the excess tax amount provided it meets conditions entailing twofold discrimination, since they:
- make adjustment of the withholding amount possible on the basis of shareholder's residence thereby excluding European companies controlled by non-French residents,
- introduce unfavorable treatment of French branches of European companies as well as the subsidiaries of said companies insofar as the branches are subjected to a presumption of distribution even in the absence of effective distribution.

4. French Victims of Discrimination

One example of French resident companies rather than foreign residents being 'victimized' by the legislation of their own country is offered with the insurance sector, where there are two different tax regimes in coexistence regarding the special tax on insurance policies. Depending on their status, even though companies may be similar with regard to their market offers and activities conducted, they may not necessarily receive equal treatment, i.e. benefit of exemption from this special tax.

This leads to the consideration that whilst an international treaty cannot restrict the tax sovereignty of France, on the other hand a treaty at the European level could entail internal discrimination prejudicial to French insurance companies through application of the more favourable regime to enterprises of another Member State by virtue of their status according to French insurance regulations.

Conclusion

In France as in most countries, non-residents are not treated the same as residents. This seems to be a structural fact-of-life of international fiscal affairs since treaties do not fully eliminate this discrimination.

There does not appear to be at this stage of developments any solution in principle to the total elimination of discrimination tax practices, and different national tax authorities may not have homogeneous approaches either due to discrepancies in domestic doctrine or failure to coordinate on treatment of specific cases.

Yet, case law is questioning this through the principle of greater coherency between tax regimes and future progress is indeed heralded by the efforts toward greater correlation of EC goals with national implementation measures made on a case by case basis.

In closing therefore, once again emphasis should be placed on the powerful tool of new negotiations being conducted with the different judicial and administrative authorities at every opportunity, followed where necessary by the challenge of litigation. Using the founding principles of the Maastricht Treaty in this 'combat' is a promising aspect of the European harmonization process.