

Opinion Statement ECJ-TF 4/2017 on the Decision of the Court of Justice of the European Union of 9 February 2017 in X (Case “Pro-Rata Personal Deductions”), Concerning Personal and Family Tax Benefits in Multi-State Situations

This CFE Opinion Statement, submitted to the European Institutions in December 2017, comments on the ECJ decision in X (Case C-283/15).

1. Introduction

This Opinion Statement was prepared by the CFE ECJ Task Force. It concerns X (Case C-283/15), in respect of which the First Chamber of the Court of Justice of the European Union (ECJ) delivered its decision on 9 February 2017.¹ In general terms, the Court followed the Opinion of Advocate General Wathelet of 7 September 2016.²

The case concerned tax legislation permitting the deduction of “negative income” relating to a dwelling. The issue was whether the fundamental freedoms must be interpreted as precluding a Member State from refusing the benefit of that deduction in respect of a self-employed non-resident in circumstances in which that person receives 60% of his total income within that Member State, and 40% within a non-Member State. Therefore, he does not receive income that enables him to qualify for an equivalent right to deduct within the Member State where his dwelling is located.

Having recognized that the freedom of establishment applies to the case, the First Chamber confirmed the right of that person to a deduction of “negative income” relating to his dwelling. Subsequently, it held that a self-employed person can claim an equivalent right of deduction in any Member State of activity within which that person receives income, in proportion to the share of that income received within each Member State of activity.

A “Member State of activity” is any Member State that has the power to tax such income from the activities of a non-resident as is received within its territory, irrespective of where the activities are actually performed.

Finally, the Court stated that the fact that the non-resident taxpayer concerned receives part of his taxable income within a third country rather than a Member State is not relevant.

2. Background and Issues

The Court’s decision in X³ adds another decision to the extensive body of case law on the *Schumacker* (Case C-279/93)⁴ doctrine, which, however, has not dealt with a situation in which a taxpayer earns income in several source states. By expanding that doctrine to multi-state situations, the decision in X obliges all source Member States to grant personal and family benefits on a pro-rata basis in the absence of sufficient taxable income in the taxpayer’s residence state.

The case concerned the year 2007: X is a non-resident national of the Netherlands who owns a dwelling located in Spain, his only state of residence.⁵ In the taxable year at issue, he derived income from professional activities from two companies in which he holds majority shareholdings, one of which is established in the Netherlands and the other in Switzerland. The income from the Netherlands source represented 60% of his total taxable income, and the income from the Swiss source 40%. In accordance with the applicable tax treaties, the income from the Swiss source was taxed in Switzerland and the income from the Netherlands source in the Netherlands.⁶ He did not receive any income taxable in Spain in 2007,

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1. NL: ECJ, 9 Feb. 2017, Case C-283/15, *X v. Staatssecretaris van Financiën*, ECJ Case Law IBFD.
2. NL: Opinion of Advocate General Wathelet, 7 Sept. 2016, Case C-283/15, *X v. Staatssecretaris van Financiën*, ECJ Case Law IBFD.

3. The ECJ Task Force notes the increasing number of “X” or similarly anonymized cases, with two – Cases C-283/15 and C-317/15 – even decided in the same month. This makes it hard to identify the specific case and for this reason the authors suggest that the technical matter it addresses also be referred to, for example, “pro-rata personal deductions” in the present case.
4. DE: ECJ, 14 Feb. 1995, Case C-279/93, *Finanzamt Köln-Altstadt v. Roland Schumacker*, ECJ Case Law IBFD.
5. X (C-283/15), para. 10.
6. X (C-283/15), para. 12.

or in the four subsequent years, after which X ceased to be resident in Spain.⁷

Under the Netherlands Income Tax Act 2001 (ITA 2001),⁸ taxable income for residents not only includes income from work, but also notional income from a primary dwelling that is owned by the taxpayer. The gross income from a residence is calculated as a percentage of the value of the dwelling. From that gross notional income expenses may be deducted, including interest and costs arising from debts incurred in acquiring the dwelling. If the amount of those expenses exceeds the value of the “advantages”, the taxpayer is in a situation of “negative income”. Under Netherlands rules, this notional income can only be negative or zero. This can be set off against other income or will increase losses available for carry forward. Generally, non-residents do not have this negative notional income.

As regards the fundamental freedoms in such a situation, the Netherlands courts acknowledge the ECJ’s case law that “negative income” relating to immovable property located in the Member State of which a taxpayer is a resident forms a tax advantage linked to his personal situation, which is relevant to the assessment of his overall ability to pay.⁹

Therefore, in the current case, the Supreme Court of the Netherlands (*Hoge Raad*) had doubts as to the scope of the *Schumacker* case law¹⁰ because X did not receive all, or almost all, of his family income in a single Member State, other than that of his residence, which has the power to tax that income and which could, therefore, take into account his personal and family circumstances. The Court’s decisions in *Gschwind* (Case C-391/97),¹¹ *de Groot* (Case C-385/00)¹² and *Commission v. Estonia* (Case C-39/10)¹³ can be read, in the opinion of the referring *Hoge Raad*, as meaning that the Member State where an activity is carried out must always take into account the personal and family circumstances of the person concerned if the Member State of residence is not in a position to do so.¹⁴

The Supreme Court’s preliminary questions were:

(1) Must the provisions of the FEU Treaty relating to free movement be interpreted as precluding national legislation under which a European Union citizen who resides in Spain and whose work-related income is taxed in the amount of approximately 60% by the Netherlands and approximately 40% by Switzerland

may not deduct from his work-related income, which is taxed in the Netherlands, his negative income arising from his dwelling in Spain, which is owned by him for his personal use, even if he receives such a low income in Spain, as his State of residence, that the abovementioned negative income could not have led to tax relief in the tax year in question in the State of residence?

(2) (a) If Question 1 is answered in the affirmative: must every Member State in which the European Union citizen earns part of his income take into account the full amount of the abovementioned negative income? Or does that obligation apply to only one of the States concerned in which work is carried out, and if so, to which? Or must each of the States in which work is carried out (not being the State of residence) allow part of that negative income to be deducted? In the latter case, how is that deductible part to be determined?

(b) In this regard, is the Member State in which the work is actually performed the decisive factor, or is the decisive factor which Member State has the power to tax the income earned thereby?

(3) Would the answer to the two questions set out under (2) be different if one of the States in which the European Union citizen earns his income is [the Swiss Confederation], which is not a Member State of the European Union and also does not belong to the European Economic Area?

(4) To what extent is it significant in this regard whether the legislation of the taxpayer’s country of residence (in this case, Spain) makes provision for the possibility of deducting mortgage interest relating to the taxpayer’s property and the possibility of offsetting the tax losses arising therefrom in the year in question against possible income earned in that country in later years?

3. The Decision of the Court of Justice

While the *Hoge Raad* did not identify a specific freedom, the Court decided that this case falls under the freedom of establishment (article 49 of the Treaty on the Functioning of the European Union (TFEU) (2007)),¹⁵ and subsequently added that the *Schumacker* doctrine, which was initially developed in the area of free movement of workers (article 45 of the TFEU), can be transposed to that freedom as well.¹⁶

In substance, the Court then established that to the extent the legislation of a Member State deprives non-resident taxpayers of the opportunity that is open to resident taxpayers to deduct negative income relating to immovable property in the state of residence (“negative income”), it treats non-residents less favourably than residents. Subsequently, it must be assessed whether this different treatment constitutes discrimination.¹⁷

The Court held that, in respect of the tax advantage of taking into account “negative income”, the mere fact that a non-resident may have received, within the Member State where his activity is performed, income on condi-

7. X (C-283/15), para. 11.
8. NL: Wet inkomstenbelasting 2001 [Income Tax Act 2001 (ITA 2001)], National Legislation IBFD.
9. Based on, for example, LU: ECJ, 18 July 2007, Case C-182/06, *État du Grand Duchy of Luxembourg v. Hans Ulrich Lakebrink and Katrin Peters-Lakebrink*, EU:C:2007:452, ECJ Case Law IBFD; NL: ECJ, 16 Oct. 2008, Case C-527/06, *R. H. H. Renneberg v. Staatssecretaris van Financiën*, EU:C:2008:566, paras 64-71, ECJ Case Law IBFD; and NL: ECJ, 18 June 2015, Case C-9/14, *Staatssecretaris van Financiën v. D.G. Kieback*, EU:C:2015:406, para. 19, ECJ Case Law IBFD; see also X (C-283/15), para. 26.
10. Starting with *Schumacker* (C-279/93).
11. DE: ECJ, 14 Sept. 1999, Case C-391/97, *Frans Gschwind v. Finanzamt Aachen-Außenstadt*, EU:C:1999:409, ECJ Case Law IBFD.
12. NL: ECJ, 12 Dec. 2002, Case C-385/00, *F.W.L. de Groot v. Staatssecretaris van Financiën*, EU:C:2002:750, ECJ Case Law IBFD.
13. EE: ECJ, 10 May 2012, Case C-39/10, *European Commission v. Republic of Estonia*, EU:C:2012:282, ECJ Case Law IBFD.
14. X (C-283/15), paras. 17-18.

15. Consolidated Versions of the Treaty on European Union and the Treaty on the Functioning of the European Union (2008/C115/01), 13 Dec.2007, OJ C115 (2008), EU Law IBFD. X (C-283/15), paras. 20-23.
16. See X (C-283/15), para. 36, referring to NL: ECJ, 11 Aug. 1995, Case C-80/94, *G. H. E. J. Wielockx v. Inspecteur der Directe Belastingen*, EU:C:1995:271, ECJ Case Law IBFD; NL: ECJ, 27 June 1996, Case C-107/94, *P. H. Asscher v. Staatssecretaris van Financiën*, EU:C:1996:251, ECJ Case Law IBFD; and DE: ECJ, 28 Feb. 2013, Case C-425/11, *Katja Ettwein v. Finanzamt Konstanz*, EU:C:2013:121, ECJ Case Law IBFD.
17. X (C-283/15), para. 27 et seq.

tions more or less similar to those of residents of that state is not sufficient to render his situation objectively comparable to the situation of the latter. In addition, it is necessary that, as a result of the non-resident receiving the majority of his income outside the Member State of residence, the Member State of residence is not in a position to grant him the advantages that accrue from taking into account his aggregate income and his personal and family circumstances.¹⁸

Furthermore, the Court held that where a non-resident receives 60% of his total global income within the Member State where he performs some of his activities, it cannot be inferred, for this reason alone, that his Member State of residence will not be in a position to take into account his aggregate income and personal and family circumstances. The Court held that this would only apply if it were established that the person concerned received, within his state of residence, either no income or such a modest amount of income that that state would not be able to grant him the advantages that would accrue from account being taken of his aggregate income and his personal and family circumstances. The Court stated that this appeared to be exactly "the situation of X, since it is apparent from the documents in the file submitted to the Court that X did not, in the tax year at issue in the main proceedings, receive any income within the Member State where he was resident, namely the Kingdom of Spain".¹⁹

The Court also clarified that this conclusion would still stand if X happened to receive the remainder of his income in that year within a state other than the Netherlands and Spain. The fact that a taxpayer receives the majority of his income from several states, other than the one wherein he is resident, as opposed to just one, has no effect on the application of the principles deriving from the *Schumacker* case law. For the Court, "the decisive criterion is whether it is impossible for a Member State to take into account, for the calculation of tax, the personal and family circumstances of a taxpayer in the absence of sufficient taxable income, although such circumstances can otherwise be taken into account when there is sufficient income".²⁰

As a result, the Court answered the first question as follows:²¹

Article 49 TFEU must be interpreted as precluding a Member State, the tax legislation of which permits the deduction of 'negative income' relating to a dwelling, from refusing the benefit of that deduction to a self-employed non-resident where that person receives, within that Member State, 60% of his total income and does not receive, within the Member State where his dwelling is located, income that enables him to qualify for an equivalent right to deduct.

In relation to the second question, the Court held that the personal and family circumstances of a taxpayer should be taken into account by granting a tax advantage in the form of reduced taxation. Consequently, the concept of a

"Member State of activity" cannot be understood as one other than a Member State that has the power to tax all or part of the income from the activity of a taxpayer, wherever the activity generating that income is actually performed.²²

The Court also stated that the freedom of the Member States to allocate among themselves their powers to impose taxes, and in particular to avoid the accumulation of tax advantages, must be reconciled with the necessity that taxpayers of the relevant Member States concerned be assured that, ultimately, all their personal and family circumstances will be duly taken into account. This should be the case irrespective of how the Member States concerned have allocated that obligation amongst themselves. If such reconciliation does not take place, the freedom of Member States to allocate the power to impose taxes amongst themselves would be liable to create inequality of treatment of the taxpayers concerned, which would be incompatible with the freedom of establishment. That inequality would not be the result of disparities between the provisions of national tax law.²³

In a situation in which a self-employed person receives his taxable income within a number of Member States, other than his state of residence, that reconciliation can be achieved only by permitting him to submit a claim for his right to deduct "negative income" to each Member State of activity where that type of tax advantage is granted, in proportion to the share of his income received within each such Member State. The taxpayer is responsible for providing the competent national authorities with the information on his global income required by them to determine that proportion.²⁴

Hence, the Court answered the second question as follows:²⁵

[T]he injunction imposed by the answer to the first question concerns any Member State of activity within which a self-employed person receives income enabling him to claim there an equivalent right of deduction, in proportion to the share of that income received within each Member State of activity. In that regard, a 'Member State of activity' is any Member State that has the power to tax such income from the activities of a non-resident as is received within its territory, irrespective of where the activities are actually performed.

The Court then held that the freedom of establishment obliges all Member States not to discriminate against a self-employed person who performs a professional activity within a Member State other than his state of residence. This obligation also applies if the taxpayer carries out the remainder of his activities within a third state, even if the latter is not a Member State.²⁶

Therefore, the Court's answer to the third question was:²⁷

[T]he fact that the non-resident taxpayer concerned receives part of his taxable income not within a Member State, but within a

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22. Id., para. 45.

23. Id., para. 47.

24. Id., para. 48.

25. Id., ruling 2 and para. 49.

26. Id., paras. 51-52, referring, by analogy, to *Kieback* (C-9/14), para. 35.

27. Id., ruling 3 and para. 52.

18. Id., paras. 37-38.

19. Id., paras. 39-41.

20. Id., para. 42.

21. Id., ruling 1 and para. 43.

non-Member State, is of no relevance to the answer to the second question.

Finally, the Court found that the last question on the effect of the (potential) deductions in Spain is inadmissible, as it is a hypothetical question.²⁸ Hence – unlike Advocate General Wathelet²⁹ – the Court did not substantively address the question of the relationship between the *Schumacker*-based consideration of a taxpayer's negative rental income and the limits on cross-border loss relief following from, for example, *Marks & Spencer* (Case C-446/03).³⁰

4. Comments

4.1. Grey, instead of black and white

With this important decision, the Court further develops its *Schumacker* case law in respect of multi-state situations, which a number of taxpayers will benefit from.³¹ This evolution, of course, only applies in the context of the free movement of workers (article 45 of the TFEU), for which the *Schumacker* line of case law was initially developed, but also with regard to the freedom of establishment (article 49 of the TFEU)³² and the free movement of capital (article 63 of the TFEU).³³ It will also be relevant in respect of the freedom to provide services (article 56 of the TFEU).

The Court continues that, in general, it is for the taxpayer's state of residence to take into account his personal and family circumstances,³⁴ which is also in line with the OECD Model (2014).³⁵ It is, moreover, settled case law, since *Schumacker*, that resident and non-resident individuals are, as a general rule, non-comparable with regard to personal and family circumstances.³⁶ The scope of the

case law arising from the decision in *Schumacker* extends to all the tax advantages connected with the non-resident's ability to pay tax that are not granted either in the state of residence or in the state of employment.³⁷ This "subjective ability to pay" is obviously viewed from a European angle (without regard to the qualification under domestic law)³⁸ and includes personal and family tax benefits, such as spousal income splitting,³⁹ tax rate benefits for retirement income,⁴⁰ the zero-rate bracket⁴¹ or tax-free allowance⁴² and the deduction of childcare costs,⁴³ but also extends to the effects of negative rental income on progressivity⁴⁴ and – as in the present case – the tax base.⁴⁵ It needs to be distinguished, however, from the Court's case law with regard to income-related expenses ("expenditure linked directly to the income of a person"⁴⁶), i.e. the "objective ability to pay", in cases such as *Gerritse* (Case C-234/01⁴⁷) and *Scorpio* (C-290/04⁴⁸), where comparability of non-resident and resident taxpayers is not in doubt when the source state exercises its taxing right over the respective income.

However, this notion of non-comparability of taxpayers with regard to their personal and family circumstances has its limits. Indeed, the Court decided that the situations of residents and non-residents can, by exception, be comparable in situations in which the Member State of residence is not in a position to grant tax advantages connected to its resident's personal and family circumstances.⁴⁹ In *Schumacker*, the Court established two (seemingly) cumulative criteria for such comparability, i.e. (1) that a person not have significant taxable annual income in the Member State of residence (so that the income is insufficient to take into account personal and family circumstances) and (2) that the taxpayer earn the major part of his taxable annual income from an activity in another

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28. *Id.*, para. 55.

29. AG Opinion in *X* (C-283/15), para. 71 et seq.

30. UK: ECJ, 13 Dec. 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, EU:C:2005:763, ECJ Case Law IBFD.

31. This development may also be relevant in the interpretation and application of the Agreement between the European Community and its Member States, of the one part, and the Swiss Confederation, of the other, on the free movement of persons (21 June 1999), EU Law IBFD. Indeed, as Advocate General Wathelet noted, the interpretation in *X* "constitutes an application of the judgment of 14 February 1995, *Schumacker* (C-279/93, EU:C:1995:31), where there are several States of activity. That judgment precedes the signature of the Agreement between the European Community and its [Member States], of the one part, and the Swiss Confederation, of the other, on the free movement of persons, signed in on 21 June 1999 (OJ 2002 L 114, p. 6; 'the Agreement'). Consequently, in accordance with Article 16(2) of the Agreement, account must be taken of that case-law" (see AG Opinion in *X* (C-283/15), para. 70, with further references in footnote 30 of the Opinion). The Court did not, however, address the question of whether or not the pro-rata application of the *Schumacker* doctrine may also be invoked against Switzerland.

32. See *X* (C-283/15), para. 36, referring to *Wielockx* (C-80/94), *Asscher* (C-107/94) and *Ettwein* (C-425/11).

33. NL: ECJ (Grand Chamber), 5 July 2005, Case C-376/03, *D. v. Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, EU:C:2005:424, para. 24 et seq., ECJ Case Law IBFD.

34. See, inter alia, *Schumacker* (C-279/93), paras. 31 and 32; *Kieback* (C-9/14), para. 22; and *X* (C-283/15), para. 30.

35. See *OECD Model Tax Convention on Income and on Capital* (26 July 2014), art. 24(3), Models IBFD, *OECD Model Tax Convention on Income and on Capital: Commentary on Article 18* para. 1 (26 July 2014), Models IBFD; paras. 41-42 *OECD Model: Commentary on Articles 23A and B* (2014); and paras. 8 and 36 *OECD Model: Commentary on Article 24*.

36. See *Schumacker* (C-279/93), paras. 31 and 32 and *X* (C-283/15), para. 30.

37. *Lakebrink and Peters-Lakebrink* (C-182/06), para. 34 and *Kieback* (C-9/14), para. 27.

38. See conversely, for example, DE: ECJ, 6 July 2006, Case C-346/04, *Robert Hans Conijn v. Finanzamt Hamburg-Nord*, EU:C:2006:445, ECJ Case Law IBFD, wherein the Court treated expenses for tax advice as income-related expenses (and applied the *Gerritse* approach), whereas such expenses were deemed to be personal under German domestic law.

39. *Schumacker* (C-279/93); *Gschwind* (C-391/97); and LU: ECJ, 16 May 2000, Case C-87/99, *Patrick Zurstrassen v. Administration des contributions directes*, EU:C:2000:251, ECJ Case Law IBFD; see also DE: ECJ, 25 Jan. 2007, Case C-329/05, *Finanzamt Dinslaken v. Gerold Meindl*, EU:C:2007:57, ECJ Case Law IBFD.

40. FI: ECJ, 9 Nov. 2006, Case C-520/04, *Pirkko Marjatta Turpeinen*, EU:C:2006:703, ECJ Case Law IBFD.

41. SE: ECJ, 1 July 2014, Case C-169/03, *Florian W. Wallentin v. Riksskatteverket*, EU:C:2004:403, ECJ Case Law IBFD; see also DE: ECJ, 12 June 2003, Case C-234/01, *Arnoud Gerritse v. Finanzamt Neukölln-Nord*, EU:C:2003:340, ECJ Case Law IBFD.

42. D (C-376/03), para. 24 et seq.

43. BE: ECJ, 12 Dec. 2013, Case C-303/12, *Guido Imfeld and Nathalie Garret v. État belge*, EU:C:2013:822, ECJ Case Law IBFD.

44. *Lakebrink and Peters-Lakebrink* (C-182/06).

45. *Renneberg* (C-527/06).

46. See, for this terminology, for example, *Conijn* (C-346/04), para. 20.

47. *Gerritse* (C-234/01).

48. DE: ECJ, 3 Oct. 2006, Case C-290/04, *FKP Scorpio Konzertproduktionen GmbH v. Finanzamt Hamburg-Eimsbüttel*, EU:C:2006:630, ECJ Case Law IBFD.

49. *Schumacker* (C-279/93), paras. 36-38; *De Groot* (C-385/00), para. 89; *Wallentin* (C-169/03), paras. 17-18; *Kieback* (C-9/14), paras. 24-35; and SE: ECJ, 19 Nov. 2015, Case C-632/13, *Skatteverket v. Hilkka Hirvonen*, ECLI:EU:C:2015:765, para. 31, ECJ Case Law IBFD; and *X* (C-283/15), paras. 32-38.

(Member) State,⁵⁰ which was often understood to be a "strict" limit of approximately 75%⁵¹ or 90%⁵² of worldwide income. It should also be noted, however, that these percentages were included in the domestic tax laws concerned and that the Court left room for other approaches.⁵³ These cumulative criteria were also reiterated in more recent decisions, such as the 2013 case of *Imfeld and Garret* (Case C-303/12).⁵⁴ From subsequent case law, it is also clear that the state of residence's ability to take personal and family circumstances into account is to be determined under the legislation of that state.⁵⁵ Therefore, if the state of residence exempts certain income from taxation and hence cannot grant personal and family benefits, the source state is not relieved of its *Schumacker* obligation.⁵⁶ (A different perspective needs to be taken, however, if the residence state does not impose a certain tax at all, for example, a wealth tax, in which circumstance the Court focuses on the overall wealth of the taxpayer).⁵⁷

This means, however, that the starting-point remains that the Member State of residence is primarily responsible for accounting for the personal and family circumstances of its residents. If, in that Member State, sufficient taxable income is earned for doing so, the situation of this taxpayer in the Member State where the activity is performed is not comparable to the situation of a resident of that state. The Court, however, based strongly on the Opinion of Advocate General Wathelet,⁵⁸ refined its *Schumacker* case law by accepting that, if the taxable income in the Member State of residence is insufficient to take into account the taxpayer's personal and family circumstances, the situation of a non-resident taxpayer in the Member State of activity, i.e. the source state, is comparable to that of a resident of that Member State.

The second *Schumacker* criterion, i.e. that the taxpayer earn the majority of his taxable annual income from an activity in another (Member) State,⁵⁹ has, therefore, been

effectively abolished and negative conflicts of competence avoided: X makes it clear that the criterion of having obtained the "major part" or "almost all" of the non-resident's taxable income from an activity performed in another Member State does not mean that this income must satisfy a certain threshold if it is otherwise impossible for the taxpayer's Member State of residence to take into account his personal and family circumstances in the absence of sufficient taxable income in that state. In this scenario, any taxable income in other (Member) States of activity is sufficient. Moreover, in this context, it does not matter whether the non-resident taxpayer receives the remainder of his income in the year concerned within a state – a Member State or a third State – other than the Member State of activity concerned and the Member State of residence. While this focus became evident in X, previous cases were already pointing in this direction: in *Kieback* (Case C-9/14), for example, the Court referred to the classical *Schumacker* situation as a mere example and made an effective causal (and not cumulative) connection between the situations in the residence and the source states.⁶⁰ Further, in *Commission v. Estonia*, the Court put an obligation on the source state to grant its personal and family tax benefits even though only approximately 50% (and not "almost all") of the income was earned there.⁶¹

The effect of that comparability is, in general, that the source Member State has to grant non-discriminatory treatment: it has to grant the non-resident taxpayer the same personal and family benefits it grants its own residents (at least proportionally),⁶² i.e. the personal and family benefits its legislation provides.⁶³ Hence, the effect and nature of potential benefits may vary greatly from state to state; in an extreme case, therefore, where the source state does not provide any personal and family benefits at all for its own residents, benefits would equally not be available for taxpayers in *Schumacker* or X positions.

4.2. Relationship with *De Groot* and *Kieback*

It may also be noted that X is compatible with *De Groot*.⁶⁴ In the latter case, the Court decided that several Member States of employment could release the state of residence from the obligation to take the taxpayer's personal and family circumstances into account. This is only possible if it is not necessary for the taxpayer's aggregate annual income to reach a minimum threshold of 90% earned in a Member State other than his Member State of residence. Therefore, the idea that the phrase "a major part" of income must be interpreted as a 90%-threshold cannot be supported despite the fact that the Court in *Gschwind*

50. See, for example, *Schumacker* (C-279/93), para. 36 and *D* (C-376/03), para. 28 et seq.

51. For the approach in Estonia, for example, see *Commission v. Estonia* (C-39/10), para. 18, and more generally for a 75% threshold art. 2(2) of the Commission's recommendation of 21 December 1993 on the taxation of certain items of income received by non-residents in a Member State other than in which they are resident, OJ L 39/22 (1994).

52. Based on, for example, *Gschwind* (C-391/97), para. 32; see also *D* (C-376/03), para. 30 ("The Court has thus allowed a Member State to make grant of a benefit to non-residents subject to the condition that at least 90% of their worldwide income must be subject to tax in that State").

53. See, for example, *Gschwind* (C-391/97), para. 32: "It follows from the foregoing that Article 48(2) of the Treaty is to be interpreted as not precluding the application of a Member State's legislation under which resident married couples are granted favourable tax treatment such as that under the splitting procedure whilst the same treatment of non-resident married couples is made subject to the condition that at least 90% of their total income must be subject to tax in that Member State or, if that percentage is not reached, that their income from foreign sources not subject to tax in that State must not be above a certain ceiling, thus maintaining the possibility for account to be taken of their personal and family circumstances in the State of residence".

54. *Imfeld and Garret* (C-303/12), para. 44.

55. See, for example, *Commission v. Estonia* (C-39/10), para. 53.

56. *Wallentin* (C-169/03).

57. See *D* (C-376/03), para. 24 et seq.

58. AG Opinion in X (C-283/15).

59. See, for example, *Schumacker* (C-279/93), para. 36.

60. See *Kieback* (C-9/14), para. 25, noting that comparability "is the case particularly where a non-resident taxpayer receives no significant income in his Member State of residence and derives the major part of his taxable income from an activity pursued in the Member State of employment, so that the Member State of residence is not in a position to grant him the advantages which follow from the taking into account of his personal and family circumstances".

61. *Commission v. Estonia* (C-39/10).

62. See *infra* sec. 4.3.

63. See also, for example, X (C-283/15), para. 48.

64. *De Groot* (C-385/00), paras. 100, 102.

specifically used that threshold.⁶⁵ If the 90% threshold were, indeed, a hard criterion on its own, a taxpayer's personal and family circumstances may not always be taken into account. Such a result would be inconsistent with the ability-to-pay principle, the direct-benefit principle, an open-market economy with free competition, the efficient allocation of production factors, tax neutrality, the establishment of a level playing field, international tax neutrality, capital and labour import neutrality and origin-based taxation. Such a condition would hamper the development of the internal market. Therefore, the refinement given by the Court in *X* matches perfectly with its role as a protector of the establishment of the internal market.

However, *X* seems to conflict with *Kieback*, which related not to proportions of annual income in various countries but rather to the timing of such proportions and the taxpayer's change of residence. In *Kieback*, the Court held that no discrimination arises in the event of successive or simultaneous employment activities in several countries after a change of residence because the Member State where the non-resident taxpayer pursued his activity before leaving is not in a better position than his new state of residence to assess his personal and family circumstances.⁶⁶ A Member State from which, during only part of the taxable year, a part (but not the major part) of his annual income is received is not bound to grant the same advantages as those granted to residents.⁶⁷ The result in *X* strongly conflicts with the result in *Kieback*: Mr *Kieback*'s "negative income" from his owner-occupied house located in Germany over the period from 1 January until 31 March 2005 could not be taken into account in any of the states involved. In 2005, he left for the United States to reside and work there. Until 31 March 2005, he lived in Germany and worked as an employee in the Netherlands. The "negative income" could not be taken into account in the United States (no tax jurisdiction during the period concerned), in Germany (no income), or in the Netherlands (non-resident status). If Mr *Kieback* had been a Netherlands resident, he would have been entitled to fully deduct this amount from his employment income during the period from 1 January until 31 March 2005.⁶⁸ The *X* decision could be a reason to reconsider *Kieback*, as the Court may have overlooked the fact that tax liability in the United States only started on 1 April 2005. In general, a state does not take into account any income, positive or negative, that is received in a period before tax liability commences. As a consequence, it is more than likely that Mr *Kieback* was not able to take into account, in the United States, the "negative income" from his home in Germany received during the period from 1 January 2005 to 31 March 2005.

4.3. Effect: Pro-rata allocation

In a situation in which not taking into account the personal and family circumstances of a non-resident taxpayer

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65. *Gschwind* (C-391/97), para. 32.
 66. *Kieback* (C-9/14), para. 29.
 67. *Kieback* (C-9/14), paras. 30-34.
 68. See art. 3.1 ITA 2001.

constitutes discrimination, the Court has decided that Member States must permit a non-resident taxpayer to take into account his personal and family circumstances on a pro-rata basis, i.e. grant the personal and family tax benefits "in proportion to the share of that income received within each Member State of activity".⁶⁹ The latter notion – "Member State of activity" – is to be understood from a tax perspective: it is not necessarily the state in which the taxpayer's income-generating activity is actually performed, but rather "any Member State that has the power to tax such income from the activities of a non-resident as is received within its territory".⁷⁰ This approach should be supported: only states that can and may tax the income of a taxpayer under their domestic tax laws or tax treaties can grant tax advantages connected with the non-resident taxpayer's personal and family circumstances. If a state cannot or may not tax his income, it simply cannot take into account the taxpayer's personal and family circumstances for tax purposes.

As the Court decided in *X*, the obligation to take into account a taxpayer's personal and family circumstances is "in proportion to the share of that income received within each Member State of activity" and hence does not only fall on one of the source Member States concerned in which taxable income is earned (for example, the state where most of the income is earned). Indeed, all of the relevant states contribute to the taxpayer's ability to pay taxes; in each of those states, the taxpayer benefits from the state's infrastructure to create his wealth. The taxpayer competes in all of those states in an open market. From this perspective, the Court is right in obliging them all to take into account the taxpayer's personal and family circumstances, and not just one of them. However, the fraction of benefits to be granted should not logically be determined by reference to the proportion of worldwide income that *may be taxed* in any given state, but by reference to the proportion that that state *actually imposes a tax on*. Furthermore, the Court did not establish a complete system of "fractional taxation" under which each Member State (including the state of residence) grants benefits only in proportion to its share of the taxable income (even though Member States could establish such a system),⁷¹ but rather it imposes a pro-rata obligation on source Member States if – and only if⁷² – the residence Member State cannot grant personal and family benefits.

As previously noted in section 3.1., where the pro rata system applies, each source Member State has to apply its own system of taking into account personal and family circumstances in a non-discriminatory manner,⁷³ irrespective of whether this is done through a personal allowance, a deduction, a tax credit, a general lower tax rate or any other form of relief. From a more technical perspec-

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69. *X* (C-283/15), para. 44 et seq.

70. *X* (C-283/15), para. 45.

71. *De Groot* (C-385/00), paras. 100-101.

72. See *supra* sec. 4.1. of this Opinion Statement.

73. See also *X* (C-283/15), para. 48 (noting that the taxpayer may "submit a claim for his right to deduct 'negative income' to each Member State of activity where that type of tax advantage is granted, in proportion to the share of his income received within each such Member State").

tive, however, the question arises as to how personal and family circumstances should proportionally be taken into account. This issue was not explicitly addressed in X. A practical approach is that each of the relevant states in which any of the non-resident taxpayer's taxable income is earned should take a part of the taxpayer's personal and family circumstances into account, provided the domestic tax system does so for a resident taxpayer. For example, if a taxpayer's personal and family circumstances are taken into account by means of a deduction from his taxable income, the personal allowances can be taken into account according to the proportion of the taxable source state income to the aggregate annual taxable income earned in each state (i.e. worldwide income) before benefits are granted. Moreover, as "income" is not defined by EU law, each source Member State needs to calculate the amounts of (domestic and worldwide) "income" in accordance with its own tax laws. In multi-state situations, therefore, there is likely not one fraction, but rather multiple fractions, that may vary according to the domestic income definitions of the source states involved. As a consequence, the sum of the fractions calculated by each source Member State may not add up to 100%, suggesting the possibility of an "incomplete" granting of benefits. That result, however, will be purely the consequence of different income definitions. This is a textbook example of a disparity that the fundamental freedoms are unable to address.

For a Member State to apply the pro rata approach in accordance with X, it needs information about the taxpayer's income in other Member States and also third countries in order to assess the taxpayer's worldwide income (the denominator in the fraction). This problem is not entirely new and existed already in classical two-state *Schumacker* situations (where it had to be established in the source state that the "major part" or "almost all" of the non-resident's taxable income was earned there, i.e. by demonstrating that no significant taxable income was earned anywhere else). The issue may become even more nuanced in multi-state situations. Instead of focusing on exchange of information between Member States, however, the Court merely stated that it is the taxpayer's responsibility "to provide to the competent national authorities all the information on his global income needed by them to determine that proportion".⁷⁴

The Court also acknowledged the interest of Member States "to avoid the accumulation of tax advantages".⁷⁵ Therefore, any source Member State in which only a part of the taxpayer's aggregate annual income is earned, need not take into account the full amount of that taxpayer's personal and family circumstances (for example, negative rental income). If the full amount were to be allowed as a deduction, a substantial risk of double deduction (or a "double dip") would exist. Such a double dip would also not be in line with the core ideas of the internal market.⁷⁶

However, implementing such an approach and avoiding granting isolated "advantages" to non-residents (for example, personal and family tax benefits) without the corresponding "disadvantages" that residents face (for example, progressivity based on worldwide income) will pose certain challenges for domestic legislators. While such "disadvantages" under residence-based taxation are certainly not a good reason to deny non-residents (proportionate) personal and family tax benefits,⁷⁷ the Court's decisions in *Gielen* (Case C-440/08)⁷⁸ and *Hirvonen* (Case C-632/13)⁷⁹ seem to imply that an option granted to non-residents to be taxed like residents (with the corresponding personal and family tax benefits) is not in itself sufficient to comply with the fundamental freedoms. Indeed, in X, the taxpayer had initially exercised such an election but withdrew it subsequently in light of the ensuing heavier taxation,⁸⁰ but that does not seem to have had any effect on the Court's holding. It seems strange that offering an option to be treated as a resident would not be sufficient to comply with EU law, as it is neither in the interest of taxpayers nor tax administrations to always require all non-residents from other Member States to declare their worldwide income to the source state just to comply with *Schumacker* and X (and, for example, tax them under a progression scheme).

5. The Statement

The Confédération Fiscale Européenne welcomes the pro-rata approach to personal and family deductions developed in the X decision. In doing so, the Court contributes to the establishment of the internal market. Indeed, the pro-rata approach supports an open market economy with free competition, an efficient allocation of production factors, tax neutrality, a level playing field, international tax neutrality, the ability-to-pay principle, the direct benefit principle and origin-based taxation.

The Confédération, however, also notes that implementation of the principles established by X will pose a number of technical and policy issues for domestic legislators that have not yet been addressed by the Court. These include the calculation of the relevant proportions of income and possible mechanisms to avoid "cherry picking" by non-residents.

77. See specifically *De Groot* (C-385/00), paras. 70-71.

78. NL: ECJ, 18 Mar 2010, Case C-440/08, *F. Gielen v. Staatssecretaris van Financiën*, EU:C:2010:148, para. 50 et seq., ECJ Case Law IBFD.

79. *Hirvonen* (C-632/13), para. 42.

80. See X (C-283/15), para. 14, wherein it is noted that based on the taxpayer's option to be treated in the same way as resident taxpayers "[t]he total tax thus calculated was greater than that which X would have had to pay if he had not exercised the option of being treated in the same way as resident taxpayers, with consequent taxation in Switzerland with respect to the income received in that State, namely 40% of his total income, and if he had, in addition, been permitted to deduct in its entirety the 'negative income' arising from the dwelling owned by him and located in Spain".

74. X (C-283/15), para. 48.

75. X (C-283/15), para. 47.

76. *De Groot* (C-385/00), paras. 100-102; see also X (C-283/15), para. 47.