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Opinion Statement of the CFE ECJ Taskforce on the judgment in the case of

Belgium SPF Finance V. Truck Center SA (Case C-282/07)

Judgment of 22nd December 2008

**Paper submitted by the
Confédération Fiscale Européenne
to the European Institutions
in February 2009**

This is an Opinion Statement on the ECJ judgment of Belgium SPF Finance V. Truck Center SA, Case C-282/07, Judgment of the 22nd December 2008¹. This Opinion Statement is prepared by the ECJ Taskforce² of the Confédération Fiscale Européenne (CFE). The CFE is the leading European association of 32 national tax advisory organisations representing over 180,000 tax advisers.

1. At first sight, the judgment of the ECJ in “Truck Center” might be thought to have a broad significance for the compatibility with Community Law of withholding taxes on payments of interest to non-residents. However, on a closer analysis it is clear that the case should be regarded as one which turned on a number of rather unique factors.³ As such, the case is best regarded as a singularity and of little general significance.

2. The CFE Taskforce has given its attention to this case specifically because it might have been thought to support a general principle of withholding tax on interest paid cross-border within the European Union. The Taskforce considered it important to highlight that the case should not be treated as authority for that principle. This is of particular significance to tax advisers throughout Europe as national revenue authorities might otherwise reach an erroneous conclusion about the case.⁴

¹ The judgment is by the Fourth Chamber: Judges Lenaerts (President), von Danwitz, de Lapuerta (Rapporteur), Arestis and Malenovský; Advocate General Kokott. It is notable that the decisions in LIDL Belgium (Case C-414/06, judgment of 15th May 2008) and Krankenheim Ruhesitz am Wannsee (Case C-157/07, judgment of 23rd December 2008) was also issued by the Fourth Chamber with Judge Lenaerts presiding and Judge de Lapuerta as Judge Rapporteur. The task force has commented on the former and intends to comment on the latter case in connection with a statement on cross-border loss relief.

² Members of the taskforce who took part in discussion of this case were: Stella Raventos Calvo, Isabelle Richelle, Philip Baker, Michael Lang, Franck Le Mentec, Albert Raedler and Friedrich Rödler. The views expressed in this statement do not necessarily represent the views of individual members of the taskforce or of organisations with which any of the members are associated.

³ These factors include the following: a) the ECJ considered there was no cash-flow disadvantage; b) Belgium required tax to be paid by the borrower on interest accrued and not just on interest paid; c) there was no information about any expenses of the lender; d) there was virtually no information about the taxation in the other state (Luxembourg); e) the issue had been superseded by the Interest and Royalties Directive; f) the provision for elimination of double taxation in the DTC was non-standard.

⁴ The point should again be emphasised that the specific issue in the case is now covered by the Interest and Royalties Directive, Council Directive 2003/49.

The facts and the reference to the ECJ

3. The facts of the case are quite straightforward. Truck Center was a company incorporated and resident in Belgium. It was owned as to 48% by a company incorporated and resident in Luxembourg, Wickler Finances. In February 1992, Wickler Finances lent Truck Center BEF 50m. (approximately €1.25m.), on which interest was payable. During the years from 1994 to 1996, interest on the loan was accrued in its accounts by Truck Center, but not actually paid over.⁵
4. In those years, under Belgian law, withholding tax⁶ was due on interest payable to a non-resident, but no withholding tax was due on interest payable to a resident company (or a Belgian permanent establishment of a non-resident company).⁷ The obligation to withhold tax applied to interest accrued, and was not limited to interest actually paid.⁸ Truck Center failed to pay over such tax on the interest it had accrued. In those years, a Belgian-resident company receiving interest would have been liable to corporation tax at rates of between 28% and 39%.⁹ Under the Belgium-Luxembourg Double Taxation Convention (“the DTC”), the tax at source on interest payable by a

⁵ The fact that interest was entered in the accounts but not paid over is stated very clearly both in the Judgment of the ECJ, at para. 13 and the Opinion of Advocate General Kokott at para. 9.

⁶ The term “withholding tax” is used here, though - to clarify - this is not a separate tax. The liability was to Belgian income tax, which was the liability of the non-resident who received income from a source in Belgium; the payer was obliged to withhold and pay over to the Belgian revenue authorities an amount on account of that non-resident’s liability to tax.

⁷ This was due to an exemption from withholding tax for payments to resident companies contained in the Belgian legislation – the exemption is explained in the Judgment at paras. 6 and 7, and the Opinion of the Advocate General at para. 7. The question referred by the Court of Liège focused on this exemption and the provisions of the DTC, and asked if the exemption taken together with the provisions of the DTC on interest infringed Community law. Thus the ECJ may have been pointed in the direction of examining the tax position of the recipient and the DTC provision by the wording of the question referred to it.

⁸ This has some resonance with the Commentary to Article 11 of the OECD Commentary which states (at para. 5) that “the term ‘paid’ has a very wide meaning, since the concept of payment means the fulfilment of the obligation to put funds at the disposal of the creditor in the manner required by contract or by custom.” As explained in the Judgment (para. 5) and the Advocate General’s Opinion (para. 6), the placing of the interest in an account triggered the obligation to withhold tax, even if the beneficiary could not access that account.

⁹ See the Advocate-General’s Opinion, paragraph 67. The corporate tax rate was 39% (plus 3% complementary tax, making 41.17%); there was a reduced rate for small companies at progressive rates from 28% upwards.

resident of Belgium to a Luxembourg company owning more than 25% of its shares was limited to a maximum of 15%. Where a non-resident of Belgium received income from that country which had been subject to tax withheld on payment, the tax withheld was the final Belgian liability.¹⁰

5. In 1997, following an audit, the Belgian revenue authorities assessed Truck Center to the tax which should have been paid with respect to the interest for 1994 and 1995 at 13.39%, and for 1996 at 15%.¹¹
6. In 2005, Truck Center's challenge came before the Belgian courts, and the Court of Appeal of Liège referred a question to the ECJ for a preliminary ruling. That question asked simply the compatibility with Community Law of a withholding tax on interest paid to a resident of another member state, where no withholding tax applied on interest paid to a resident of Belgium. The ECJ concluded that the Belgian rule was not incompatible with the freedom of establishment or the free movement of capital.¹²

¹⁰ That is, the non-resident taxpayer did not have to file a Belgian tax return, and the tax withheld on the gross payment discharged the non-resident's liability to Belgian tax. It also appears that it was not possible (and is still not possible) for the non-resident to file a Belgian tax return and ask for taxation on the net amount, after deducting allowable expenses, and claim repayment of the excess tax withheld. By contrast, where a Belgian resident is subject to tax withheld at source on gross income, it does appear possible to submit a tax return and claim back any excess of tax withheld (where, for example, the taxpayer has not used up their basic exempt amount for tax purposes).

¹¹ It is notable that the rate of tax that should have been withheld was below the maximum rate fixed in the DTC for two of the years and at the DTC maximum rate for the third year. It is understood that the domestic rate of tax to be withheld on interest only rose to 15% in 1996. Thus, for all three years, the limit in the DTC was inapplicable, the domestic law rate being apparently less than or equal to the 15% DTC maximum rate. This demonstrates clearly that a) the withholding tax was imposed under domestic law, and not under the DTC; and b) that the DTC was irrelevant in this situation since the DTC ceiling had no impact. It is a little surprising that this fact appears never to have come out during the hearings.

¹² The ECJ first discussed the relevant freedom. The Belgian Court had referred to the free movement of capital, but as the withholding tax of 15% under the DTC applied only where there was a shareholding of 25% or more, the ECJ concluded that the freedom of establishment was engaged. Though necessary, this was a rather sterile discussion as there was no suggestion that there would have been any difference in the outcome no matter which of the freedoms had applied. If one considers the position a little further, however, the Belgian court may have referred to the correct freedom. First, the lender held 48% of the shares in Truck Centre; if the remaining 52% of the shares were held by an unassociated company, then the 48% would not have given Wickler Finances control (assuming actual control is necessary to satisfy the freedom of establishment's test of substantial influence). Secondly, the rates of 13.39% and 15% were the domestic rates, disregarding the treaty, then the treaty provision – and the requirement of a 25% shareholding – was entirely irrelevant: as explained, the DTC ceiling was not engaged. Finally, if the real question is whether a borrower from a non-resident company had to withhold tax on interest accrued, while a borrower from a Belgian company did not, then the key issue was the source of the loan, not the level of withholding tax: that is better seen as a free movement of capital issue.

Comments on the ECJ's decision

7. The ECJ answered the single question in a very brief fashion, with relatively little analysis. The judgment is less than convincing.

Regarding the objectively comparable situation of the Luxembourg and Belgian companies

8. After having confirmed that the freedom of establishment was applicable in the present case, the ECJ then applied a discrimination analysis (at paragraphs 36 to 48 of the Judgment) and asked if a Luxembourg company and a Belgian company receiving interest were in an objectively comparable situation. Though this follows the approach taken by the Advocate General, it is doubtful if this was the correct approach. The ECJ's approach focuses on the taxation of the lender who receives the interest. However, the question referred by the Belgian court related to the obligation of the borrower to pay over an amount in respect of tax when it accrues interest payable to a non-resident. The true comparison would have involved a discussion whether a Belgian borrower would have to pay over an amount in respect of tax when accruing interest payable to a Belgian lender. While it is correct that the tax was paid over in respect of an ultimate liability of the Luxembourg lender, the question itself¹³ referred only to the obligation imposed on the borrower to withhold tax.¹⁴

¹³ This is clear from the way that the ECJ rephrased the question at para. 21 as follows: "By its question, the referring court asks, in essence, whether Articles 73b and 73d of the Treaty preclude legislation of a Member State which provides for the retention of tax at source on interest paid by a company resident in that Member State to a recipient company resident in another Member State, while exempting from that retention interest paid to a recipient company resident in the first Member State."

¹⁴ In fact, to go further, the real comparison is with a Belgian lender that failed to withhold tax to a Luxembourg lender and a similar lender who failed to withhold tax to a Belgian lender. The failure was disclosed here in an audit procedure, and presumably involved the payment of interest and penalties. In the case of the loan from a Belgian lender, presumably there would have been no disclosure in an audit (there being no obligation to withhold in the first place), no interest and no penalties.

9. Focusing on the correct comparison is particularly significant when considering any cash flow advantages or disadvantages (discussed below).
10. If the Court had focused only on the borrower, then the analysis might have been quite simple. In the normal situation where a withholding tax is imposed on interest which is actually paid over (and not merely accrued) to the lender, the borrower is no worse off as a result of this withholding tax than if none were imposed. This is because the borrower is usually allowed to treat the tax withheld as part satisfaction of its obligation to pay interest.¹⁵ To take an example: suppose a borrower has borrowed 8,000,000 at 5% interest. The interest obligation is 400,000 per annum, or 100,000 per quarter. If there is a 15% withholding tax, then each quarter the borrower pays to the lender 85,000 and to the revenue authority 15,000: the 15,000 is paid in respect of the lender's liability to tax in the state of source, and is accepted in part-satisfaction of the obligation to pay the interest. If there were no similar withholding tax in a purely domestic situation, the borrower would simply pay the lender 100,000 – the borrower is no worse off.¹⁶
11. The position is different, however, where – as in the facts of this case – the withholding tax is imposed on interest which is accrued but not paid. In that scenario, the borrower must pay the 15% withholding tax to the revenue authority, even though it pays nothing to the lender; this is different from the purely domestic situation where there is no withholding tax so that the borrower pays nothing (neither to the revenue authority nor to the lender).
12. The critical, and special factor in the Truck Center case was that the withholding tax was imposed on interest accrued, while there would have been no such tax liability on the borrower if the lender was a Belgium resident. That was a special feature of

¹⁵ We ignore the possibility that the loan agreement might have a gross-up clause by which the borrower agrees to pay the same amount, net of any tax withheld, as if there was no withholding tax. Such a clause will always make a cross-border borrowing more expensive than domestic borrowing where there is no withholding tax: it raises interesting questions of how far private agreements may create a situation which is incompatible with the fundamental freedoms.

¹⁶ In fact, the cross-border borrower may be slightly better off if, for example, the tax withheld need only be paid over to the revenue authority say 14 days after the interest was paid. The borrower then has 14 more days use of the tax funds.

this case and it was, one suspects, the reason why Truck Center raised the issue of Community law in the first place.¹⁷

13. Thus the answer the Court should have given, on a correct analysis of the issue and the question actually posed, was this: it is not incompatible with the free movement of capital (or the freedom of establishment) to impose a withholding tax obligation on a borrower who actually pays (and does not merely accrue) interest to a non-resident, even when there is no withholding tax on payment of interest to a resident lender. However, it is not compatible to impose a withholding tax on interest which is accrued (and not actually paid over) to a non-resident where there is no equivalent withholding tax on interest accrued to a resident lender.¹⁸

14. The Court however, did not take this route, but focused on the tax position of the lender. The Court began its analysis by noting that the situations of residents and non-residents are, as a rule, not comparable (see paragraph 38). With respect to individuals, the ECJ's jurisprudence has significantly developed on this point since the

¹⁷ Again it is worth noting that it was not the lending company that received the interest that was complaining to the Belgian courts or the ECJ. The Luxembourg lender might have complained that it suffered a disadvantage when compared to a Belgian lender: for example, a cash-flow disadvantage or the disadvantage of not being able to deduct its expenses in a net calculation. That would have been a situation similar to say, Gerritse (Case C- 234/01). However, that wasn't what was happening here. The lender was not the complaining party (after all, its interest had been accrued in the accounts of the Belgian company in which it had a 48% shareholding). If it suffered a disadvantage here, it was simply that the liability to tax and interest and penalties depreciated its shareholding in the Belgian company.

¹⁸ Though the question referred only asked about the borrower company and the obligation to withhold tax, a comprehensive answer would also have taken account of the position of the lender company as well. After all, both the Luxembourg lender and the Belgian borrower enjoyed the fundamental freedoms, and an ideal solution should ensure that neither suffers a disadvantage in Belgium and neither suffers from an infringement of the freedom enjoyed by itself or by its counterparty. Thus the Belgian company should not be disadvantaged because it borrowed from a Luxembourg company, or the Luxembourg company disadvantaged in Belgium (and, arguably, not in Luxembourg either) because it is a non-resident lender. Thus a truly comprehensive answer might be:

“It is not incompatible with the free movement of capital (or the freedom of establishment) to impose a withholding tax obligation on a borrower who actually pays (and does not merely accrue) interest to a non-resident, even when there is no withholding tax on payment of interest to a resident lender. However, it is not compatible to impose a withholding tax on interest which is accrued (and not actually paid over) to a non-resident where there is no equivalent withholding tax on interest accrued to a resident lender. Where a withholding tax is imposed in conformity with these principles, it is still for the national court to reassure itself that the non-resident lender is not disadvantaged under the tax system of the state of residence of the payer of the interest by comparison with a resident lender (for example, with respect to the timing of payment of tax or the effective rate of tax or the ability to deduct expenses when computing the lender's final tax liability”.

judgments in Schumacker¹⁹ and Wielockx²⁰, cited by the Court.²¹ The ECJ is not, of course, saying that it is sufficient simply that a rule applies differently to residents and non-residents: there must be some difference between the resident and non-resident which makes their positions not objectively comparable.

15. Here, at the heart of the ECJ's decision, the Court points to three differences which, according to its view, confirm that the positions were not objectively comparable.
16. First, the position of the Belgian State is different in that it taxes a Belgian resident on grounds of residence, but a Luxembourg resident in its capacity as the state of source.²² With the greatest of respect, this is simply recognising that residents are taxed on a residence basis, while non-residents are taxed on a source basis (i.e. only on income having its source in Belgium). It amounts to saying that residents and non-residents are different because residents and non-residents are different.
17. Secondly, the Belgian company receiving interest and the Luxembourg company were different because they were subject to two distinct charges which rest on separate legal bases.²³ The Belgian company was subject to corporation tax along with

¹⁹ Case C-279/93, decision of 14th February 1995.

²⁰ Case C- 80/94, decision of 11th August 1995.

²¹ One of the issues which the Court should have faced is how far the jurisprudence that has developed in respect of individuals should apply equally to companies (e.g. C-311/97 – Royal Bank of Scotland). For individuals, one of the developments of the jurisprudence is to recognise that it is only for the state of residence to grant tax reliefs that relate to the personal and family circumstances of the taxpayer; that is clearly inapplicable to companies. Similarly, company taxation may be flat-rate (or have a limited degree of progression, with a small company rate), while taxation on individuals is progressive, reflecting the ability to pay principle. Progressive tax rates require account to be taken of all income, and are more appropriate to the state of residence, while flat rate tax may be appropriate for the state of source.

²² See para. 42 of the Judgment.

²³ See paras. 43 to 46 of the Judgment. The exact wording used by the Court (in the English version) was: “On the other hand, the Belgian State retains at source withholding tax on interest paid by a resident company to a non-resident company pursuant to the discretionary power which, by virtue of the Belgium-Luxembourg Convention, the Belgian State and the Grand Duchy of Luxembourg have mutually reserved for themselves in the allocation of their powers of taxation.” In fact, this is not accurate. For the years in question, the resident and the non-resident were subject to the same corporate income tax under the Belgian Income Tax Code of 1992. The rules for taxation were basically similar, with the exception, for example, of the fact that the rate of tax on non-residents was the rate at which the payer was required to withhold tax: see Art. 248 of the Code. Also, as explained above, the withholding tax rates of 13.39% in 1994 and 1995 and 15% in 1996 were the rates under domestic law – there was no exercise of a “discretionary power”: the DTC ceiling had no application in this case as the domestic law rate did not exceed the DTC rate.

the company's other income, while the Luxembourg company was subject to withholding tax at source in accordance with the provisions of the DTC.²⁴ Looked at from the point of view of the lender, that is simply and precisely a description of the difference in treatment which is the subject of the alleged discrimination. Again, it amounts to saying that a resident and a non-resident are different because a resident and a non-resident are different.

18. Finally, a Belgian company would be different from a Luxembourg company because the Belgian company could be subject to direct recovery of tax in Belgium while recovery from a Luxembourg company required the assistance of the Luxembourg revenue authorities.²⁵ That is generally the case for resident and non-residents: in the case of a non-resident, unless tax is withheld at source (or the non-resident has other assets in the state of source, against which the tax can be levied²⁶), it can normally only be recovered through co-operation of the revenue authority of the state of residence of the recipient. Again, this amounts to saying that residents and non-residents are different because residents and non-residents are different.
19. None of the suggested differences comes even close to explaining why a resident and a non-resident are not objectively comparable.
20. If the ECJ were correct, then the logical consequence of this decision is that residents and non-residents are never in an objectively comparable position, so that it is always possible to apply different tax rules to residents and non-residents. A resident

²⁴ Without being too harsh, it is arguable that the ECJ misunderstood – once again – the way in which a double taxation convention works. The convention does not give a contracting state a right to tax, or provide a basis for tax jurisdiction, or even give a “discretionary power” (see para. 45 of the Judgment) to impose tax. The jurisdiction to impose tax is a reflection of the sovereignty of each state, and tax is always imposed under provisions of domestic law. By a tax treaty, the two contracting states agree to coordinate the exercise of their sovereignty to impose taxes (in the source state by renouncing its right to tax or by limiting that right) in order to achieve certain purposes, chiefly the avoidance of double taxation. In this case, Belgium had sovereign power to impose tax on interest having its source in Belgium; it imposed that tax under its domestic law (including the domestic-law-based procedure of collecting tax by payment by the borrower); but it agreed by the DTC to limit the exercise of that sovereignty to a maximum tax charge of 15%. This can be seen in part by the fact that in the first two years at issue – 1994 and 1995 – the tax charge was 13.39% and in 1996 the domestic tax charge was 15%; i.e. the domestic law charge never in any year reached the level where the ceiling in the DTC became relevant.

²⁵ See paras. 47 and 48 of the Judgment.

²⁶ In fact, the Luxembourg lender did have other assets in Belgium here against which enforcement could take place – viz. the shareholding in the Belgian company and the accrued interest in the accounts of the borrower.

is always potentially liable to tax on worldwide income, while a non-resident is liable to tax on local source income only; residents and non-residents may be subject to two distinct charges which may rest on separate legal bases; and recovery of tax from a non-resident (if not withheld at source) always requires the assistance of a foreign revenue authority. Such a position would clearly not be consistent with prior ECJ case law. If the reasoning of the ECJ were correct, it would be hard to see how a resident and a non-resident could ever be objectively comparable.²⁷

Regarding the lack of a disadvantage

21. In a single paragraph (paragraph 49) the ECJ adds that, in addition to the fact that the situations of the resident and the non-resident are not objectively comparable, the difference in treatment does not necessarily procure an advantage for the resident recipient. Two points are made here, both of which reflect special factors in this case.
22. First, there was said to be no cash flow advantage because Belgian companies were obliged to make prepayments of corporation tax on a similar timescale to the obligation to withhold tax on interest.²⁸ The ECJ does not explain this in detail, but it is explained more fully by the Advocate-General in her opinion at paragraph 49. The

²⁷ The point might again be made, however, that the Court was making the wrong comparison. The question referred did not raise the taxation of the non-resident recipient of the interest, but of the Belgian payer of interest who had to withhold tax in this situation but not in a domestic situation. This is different, for example, from Gerritse (Case C-234/01) or Scorpio (Case C-290/04) or Centro Equestre (Case C-345/04), all of which involved taxation of the non-resident taxpayer, and not the obligation to withhold tax on the resident payer.

²⁸ This assumes that a cash flow disadvantage may be a relevant factor, which is uncertain following the judgment in LIDL Belgium (Case C-414/06, judgment of 15th May 2008 – see the Opinion Statement of the CFE Taskforce, published in (2008) *European Taxation*)

system of advance payments of corporate tax – *versements anticipés* - is a feature of the Belgian tax system under which companies make quarterly payment on account of their tax.²⁹ Even then, the timing of the obligation is not the same: the *versements anticipés* are payable at the end of the quarter, the tax payable on interest was due 14 days after the interest was paid or accrued. Thus there might be a 2 ½ month difference in the timing of the payment. The Court's conclusion that there was no cash-flow disadvantage in practice may be seen as a unique feature of this case.³⁰

23. The cash-flow comparison also highlights how important it was for the Court to make the correct comparison. The question referred by the Belgian court asked only about the borrower's obligation to withhold tax; the comparison should have been with the timing of the cash flows for the borrower when the funds were borrowed from a Belgian lender (and not the timing of payment of tax by a Belgian lender).

24. Secondly, there was no advantage to a Belgian company since the "amount of withholding tax deducted from the interest paid to a non-resident company is significantly lower than the corporation tax charged on the income of resident companies which receive interest". This is not correct: it is not the *amount* of withholding tax which is significantly lower, but the *rate* of tax (13.39% or 15%, when compared with 28% to 39% corporation tax in the years in question). However, that shows the fallacy of looking at this question *in vacuo* without having regard to the question of whether the tax was imposed on a gross or a net basis. A 15% tax on gross interest may very well yield a significantly larger amount of tax than, for example, a 39% tax charge on net interest.

25. The whole issue of gross versus net tax base, and whether there would have been allowable expenses, is absent from the Judgment, which is another unique feature which weakens the authority of this case. The question of expenses was

²⁹ Not all Member States have a similar system; for the States represented in the taskforce, Austria, Germany and Spain have this system, as does the UK (but only for large companies).

³⁰ If one considers this further, there could have been a significant cash-flow difference. Truck Center was required to withhold tax within 14 days of accruing interest; there was no information as to when a Belgium company would have to pay tax on interest payable to it but not actually paid. If the Belgian lender did not pay tax on interest on an accruals basis (but only on a receipts basis), then the Belgium company borrowing from a non-resident lender might suffer a significant disadvantage.

discussed by the Advocate-General, but in a less than satisfactory fashion³¹. It is true that the order for reference said nothing about expenses or the deduction of expenses.³² However, it would always have been open to the ECJ to say that the national court (which could find as a fact whether there were any relevant expenses) should satisfy itself that, in practice, the tax burden on the non-resident lender was no greater than the tax burden on a Belgian-resident lender.

26. To take an example, let us suppose that Truck Center had borrowed the BEF 50m. and the interest rate on the loan was 5%, so that the Belgian company paid BEF 2,500,000 in interest per year. Suppose now that the Luxembourg parent had borrowed the BEF 50m. from a bank at 4% interest, and had an interest charge of 4% to the bank. The Luxembourg company would have had a cost of BEF 2,000,000. If the parent company were in Belgium, it would have been taxed on its net profit of BEF 500,000 at a maximum of 39%, i.e., a tax charge of BEF 195,000. However, the withholding tax at 15% on the interest of BEF 2,500,000 would have been BEF 375,000.

27. If one takes the financial outcome comparison a step further, then account should also be taken of the position in Luxembourg. In the years in question, a Luxembourg company was liable to corporation tax at 34.2%³³ on interest derived from abroad. Suppose that a Luxembourg company had borrowed BEF 50m.³⁴ from a bank at 4% and lent to a Luxembourg subsidiary, then the Luxembourg tax on the net turn on the transaction would have been BEF 171,000.

³¹ At paragraphs 70 to 71 of her Opinion she expressed the view that there are scarcely likely to be significant operating expenses in connection with loan transactions between associated undertakings. With the greatest of respect, this is not necessarily correct: it is highly likely that the parent company would have borrowed funds to lend to its Belgian subsidiary, and would have had a significant interest expense. In fact, one of the biggest problems in practice in international taxation is the imposition of withholding taxes on gross payments of interest (and sometimes also of royalties) where the recipient has borrowed (or has acquired the intellectual property by licence) and is taxed in its state of residence only on the small turn resulting.

³² Arguably, the issue of expenses was irrelevant if one focused only on the obligation to pay over tax which fell on the borrower. The borrower had no relevant expenses; it was only the lender who might have had expenses. The ECJ (and the Advocate General) having focused on the taxation of the lender, the issue of expenses was directly relevant.

³³ This was a 33% corporate income tax, plus a 1.2% surcharge. Members of the Taskforce are very grateful to Prof. Alain Steichen for supplying information about the taxation in Luxembourg

³⁴ One can ignore the difference in currencies as the Luxembourg currency and the Belgian currency were tied at parity.

28. Now suppose that the Luxembourg company had lent the same amount to a Belgian company. It would be necessary to take account of the BEF 375,000 of tax withheld in Belgium at the rate of 15%. The elimination of double taxation article in the DTC operated in a particularly unusual form, with the result that no credit was granted for Belgian tax.³⁵ Instead, the Belgian tax was a deductible expense. In the scenario assumed here, the Belgian tax would have swelled the expenses from BEF 2,000,000 to BEF 2,375,000. There would still, therefore, have been Luxembourg tax to pay on the net amount of BEF 125,000 – i.e., approximately BEF 42,500 further to pay in terms of Luxembourg tax. The overall tax bill would have been BEF 417,500 (Belgian tax of BEF 375,000 and Luxembourg tax of BEF 42,500) when the net turn to the Luxembourg parent was only BEF 500,000. An effective tax rate of 83.5%.
29. Taking this example as a base, one can ask several questions. Would a Luxembourg company have lent to another Luxembourg company or to a Belgian company? Would a Belgian company have borrowed from its Luxembourg parent or (assuming the other 52% of the shares had been held by a Belgian company) from its Belgian parent?

Points that the ECJ did not consider

30. It is worth mentioning briefly that there were a number of relevant issues, some of them discussed by the Advocate-General, which are not considered at all in the ECJ's judgment.

³⁵ This is another unique feature of the case – the provision in the DTC for elimination of double taxation was in a very different form from the standard, OECD-Model provision.

Mutual assistance in the recovery of taxes

31. The first of these is the role of provisions for co-operation between member states in the collection of foreign tax debts. In Scorpio the ECJ had expressly noted that the case preceded the extension of the Directive on Mutual Assistance in the Recovery of Duties to cover the taxes in issue³⁶. Thus, for the years in question, there was no alternative to a withholding tax by requesting assistance from the member state of residence of the recipient.
32. Similarly, the facts in Truck Center predated the extension of the Directive. However, as was noted by the Advocate-General (see paragraph 42 of her Opinion) there was a separate convention between the Benelux countries dating from 5th September 1952 on Mutual Assistance in the Recovery of Tax Claims which, on its face, would have allowed the Belgian Government to request assistance from the Luxembourg Government³⁷. The Advocate-General concludes that, even if provisions for the mutual assistance in collection of taxes were in existence, the withholding tax of tax at source was a proportionate response which would have generally saved costs both for the state of source and for the taxpayer.
33. The ECJ did not consider this aspect of the case at all. Having found that the difference in treatment was neither discriminatory nor (one assumes) restrictive, it was not necessary to consider the issue of justification or proportionality. The failure to consider this issue may again be regarded as another special feature of the case.

Tax treatment in the residence State

34. Secondly, there was no information whatsoever in the case about the tax treatment in Luxembourg, other than that there would have been no withholding tax on interest paid from a Luxembourg resident to a Belgian resident. There is an ongoing discussion as to whether, in circumstances such as this, it is appropriate to look only at

³⁶ Council Directive 76/308/EEC which was not extended to most direct taxes until Council Directive 2001/44/EC of 15th June 2001.

³⁷ It is worth noting that the database of the International Bureau for Fiscal Documentation includes that 1952 convention, but notes that its status – whether it was in force or had been abandoned – was “uncertain”.

the one country (here the country of source) or to look at the tax treatment in both countries. However, the ECJ considered the restriction on the withholding tax in Belgium under Article 11 of the DTC, and also quoted the somewhat unusual provisions of Article 23 dealing with the elimination of double taxation. In the context of a double taxation convention generally, it is essential to consider any provisions that are directed at the state of source also in the light of the equivalent of Article 23 (which is directed at the state of residence). Once one is directed to look at the state of residence, it should follow that one should also take into account the tax treatment in that state. The ECJ totally fails to consider the tax treatment in Luxembourg.

Concluding comments

35. The Advocate-General notes in the opening part of her Opinion that the facts here preceded the Interest and Royalties Directive. To that extent, this case describes a position which has been overtaken by Community legislation, a factor which also weakens the authority of the case.
36. There are two critical issues that are raised by this case. The first critical issue is whether residents and non-residents are ever or never in an objectively comparable position. The development of ECJ case law on individuals, while starting from the assumption that residents and non-residents are not objectively comparable, has become more refined and has asked whether, with respect to a particular tax rule, residents and non-residents are in practice objectively comparable. This case fails to consider that issue properly.
37. The second is whether a Member State can retain a withholding tax on cross-border payments where it has no equivalent withholding of tax on payments to a

resident. That question has two facets: a possible infringement of the fundamental freedoms with respect to the payer, and with respect to the payee. As explained above, the ECJ confuses those two issues.

38. For the payer the question is whether he is unjustifiably disadvantaged, by having to withhold and pay over the tax, by comparison with a payment to a person resident in the same state.

39. For the payee, the question is whether he is disadvantaged by comparison with a resident recipient of equivalent payments.

40. In principle, it ought to be possible to retain a withholding tax in such circumstances, but provided that the resident payer and the non-resident payee are not disadvantaged in terms of cash flow, taxation on gross or net basis, and tax rates. None of those points were addressed by the ECJ. In other words, when deciding whether, for example, the withholding tax was restrictive, the following issues would have to be addressed:³⁸

- i. If the resident payer has to withhold tax on a payment accrued but not paid when the sum is due to a non-resident, but not withhold tax on an accrual basis to a resident.
- ii. If the non-resident payee was subject to tax by withholding, while the resident recipient was subject to tax as part of its normal corporation tax assessment, were the rates, base and administration of the taxes similar, or did they operate in a way that was restrictive or discriminatory?
- iii. In particular, was there a cash flow advantage to a resident recipient when compared with a non-resident recipient?

³⁸ The Advocate General sought to address most of these issues in her Opinion. The ECJ, however, addressed few of these points.

- iv. Also in particular, was the tax imposed on the resident lower than the tax on the non-resident? In answering that question, it would not be sufficient simply to look at the headline rates, but also at factors relating to the determination of the tax base: in particular, was the resident recipient taxed on a net basis, while the non-resident was taxed on a gross basis.
- v. If there was a difference in treatment between the resident and the non-resident, did the provisions of the DTC operate to effectively remove the discrimination or the restriction?³⁹

41. Overall, there are several unique features of this case which make it a singular decision, and one that should probably be accorded very little weight as authority.

³⁹ To illustrate that the compatibility of a withholding tax with Community Law cannot be adjudicated simply in a vacuum, consider this example. Suppose that Belgium had imposed a 15% withholding tax on interest paid to non-residents, and that Belgian-resident corporations receiving interest had been liable to corporation tax at 15%. However, assume that the obligation to withhold tax and pay it over to the Belgian revenue accrued at the moment that the interest was paid, while a Belgian company receiving interest only had to pay its 15% tax some twelve months after the end of the accounting period in which the interest was received; or assume that the 15% was imposed on the gross amount of interest to a non-resident, but only on the net interest to a resident company; or assume that under the DTC Luxembourg was entitled to tax the interest without any method of relief whatsoever for tax imposed in Belgium. It is submitted that in all those situations the withholding tax would have been prima facie incompatible with Community law.