REVERSE DISCRIMINATION AND DIRECT TAXATION IN THE EU

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This paper analyses whether reverse discrimination in the field of direct taxation should held by the Court of Justice of the European Union as prohibited by European Union Law. Such analysis first addresses the concept of reverse discrimination, at the same time identifying the reasons behind the occurrence of such phenomenon in the European Union. Then, focusing on the specific field of direct taxation, an exam of the Court's doctrine of "purely internal situations" shows it to be the inevitable result of the limited scope of application of the Treaties and of the coexistence between European Union Law and the Member States' legal orders. Nevertheless, even in an area of reduced harmonization such as direct taxation, some instances of reverse discrimination are in fact prohibited, should Member States try to hinder their nationals' exercise of European Union rights.

Este trabalho analisa se a discriminação invertida na área da tributação directa deverá ser considerada pelo Tribunal de Justiça da União Europeia como proibida pelo Direito Comunitário. Essa análise começa pela abordagem do conceito de discriminação invertida, simultaneamente identificando as razões subjacentes à ocorrência deste fenómeno na União Europeia. Seguidamente, focando-se especificamente na área da tributação directa, um exame da doutrina jurisprudencial de "situações puramente internas" mostra ser a mesma o resultado inevitável do campo de aplicação limitado dos Tratados e da coexistência entre o Direito da União Europeia e os ordenamentos jurídicos dos Estados Membros. Não obstante, mesmo numa área de reduzida harmonização como a da tributação directa, algumas situações de discriminação invertida são de facto proibidas, caso os Estados Membros tentem contrariar o exercício pelos seus nacionais dos respectivos direitos de matriz comunitária.

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I – INTRODUCTION

The term "discrimination" conveys an idea of detrimental treatment that is unreasonable and inherently unjust. It is generally seen as hindering the fundamental principle of equality enshrined in any normative theory of social justice[1]. Accordingly, at least from a political perspective, it appears discrimination is only to be acceptable when some differentiation or distinction is needed to attain

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[1] See A. Sen, *The Idea of Justice* (London: Allen Lane, 2009), p. 293.

substantial over formal equality. In any other instances, it seems, discrimination is as a matter of principle to be rejected[2].

The purpose of this study is to analyse whether, as some scholars argue[3], reverse discrimination in the field of direct taxation should be looked at by the Court of Justice of the European Union ("CJEU") as a measure prohibited by the Law of the European Union ("EU"). Under such view, the principle of non-discrimination on the grounds of nationality, as a vital concept of EU Law, should also inhibit Member States from discriminating against their own nationals. Reverse discrimination is seen as impairing the fundamental principle of equality within the EU, a fact even more intolerable since the creation of EU citizenship[4].

Under such approach, the CJEU case law on the scope of EU Law is deemed as unsatisfactory and outdated. In particular, the Court's doctrine of "purely internal situations" is seen as condoning great inequality among EU citizens, it being identified as at the root of reverse discrimination. Accordingly, for these Authors:

> It is possible for the ECJ to reject reverse discrimination and remove it from Community law even in the absence of harmonization on the subject matter [*i.e.* taxation] by interpreting differently some provisions of the Treaty, particularly Article 12 [now article 18 TFEU], the fundamental freedoms articles, the section on Citizenship, and Article 87 [now article 107 TFEU][5]

Our analysis will first try to attain a definition of reverse discrimination, at the same time identifying the reasons behind the occurrence of such phenomenon in the EU. One will then proceed to examine the much criticised CJEU doctrine of "purely internal situations", assessing its justifiability regarding reverse discrimination and focusing on the specific field of direct taxation.

II – REVERSE DISCRIMINATION IN THE EU

The term reverse discrimination generally describes the unwanted result of positive discrimination measures. These are measures designed to promote substantial equality at the expense of formal equality. In a nutshell, they act through securing a more beneficial treatment to a certain

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[2] For a general overview of the subject of discrimination see L. Willmore, "Discrimination", in *Report on the World Social Situation 1997* (New York: United Nations, 1997), pp. 153.

[3] Notably D. Garcia, "Are there reasons to convert Reverse Discrimination into a Prohibited Measure?", *EC Tax Review* 2009, no. 4, pp. 179-191. For a broader approach to the subject, also regarding reverse discrimination as a difference in treatment that falls within the scope of EU Law, see A. Tryfonidou, *Reverse Discrimination in EC Law* (Alphen aan den Rijn: Wolters Kluwer, 2009), pp. 129-215.

[4] Specifically on the impact of EU citizenship on the admissibility of reverse discrimination, see A. Tryfonidou, "Purely Internal Situations and Reverse Discrimination in a Citizen's Europe: time to "reverse" Reverse Discrimination?", in *Issues in Social Policy: a new agenda*, ed. P. Xuereb (Valletta: Progress Press, 2009), pp. 11-29.

[5] D. Garcia, *supra* n. 3, p. 191.

generally disfavoured group so as to compensate for an existing inequality. Sometimes, however, the benefit granted ends up outweighing the inequality sustained by the supposedly disfavoured group. Whenever that happens, it is the group theoretically better-off that actual finds itself being discriminated against. In other words, it becomes a victim of reverse discrimination.

In an EU context, reverse discrimination is typically identified with the lesser treatment by a Member State of its own nationals by comparison with the treatment conferred to nationals of other Member States. Characteristically, such lesser treatment is the result of EU rules in place that, within their general purpose of fostering the European Internal Market and pursuing the other EU goals detailed in article 3 of the Treaty on European Union ("TEU")[6], offer protection to nationals of other Member States neglecting the own nationals of the Member State governing a particular situation. Reverse discrimination in the EU has therefore the peculiar trait of being, not so much the result of positive discrimination measures, as the by-product of rules aiming to accomplish EU goals[7].

It is worth noticing that a precondition for any discrimination (including reverse discrimination) is the existence of at least two separate sets of rules governing similar situations. The fact that the EU legal framework entails the coexistence of the EU legal order with different, non-harmonised, National legal orders creates from the onset a propitious environment for differences in treatment of similar situations to occur.

Naturally such differences in treatment are a major hindrance to the establishment of a properly functioning internal market. In fact, one of the EU's most significant tasks over the years has unquestionably been to align and harmonize legislation seeking equality within the internal market.

Those efforts, however, can only go so far and in some cases face almost overwhelming difficulties. This is particular so in the matter of direct taxation, where the degree of legal integration is still minute. In fact, contrasting with indirect taxes[8], the approximation of direct tax provisions is not even expressly foreseen in the TFEU's chapter devoted to tax matters[9]. Such approximation seems bound to be achieved only through the special possibility laid down in article 115 TFEU, under which the Council, acting unanimously, may issue directives for the approximation of direct tax laws of the

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[6] As quite rightly K. Borchardt points-out, the actual *"list of tasks entrusted to the EU strongly resembles the constitutional order of a state. These are not the narrowly circumscribed technical tasks commonly assumed by international organizations, but fields of competence which, taken as a whole, form essential attributes of statehood. The list of tasks entrusted to the EU is very wide-ranging, covering economic, social and political action. The economic tasks are centered around establishing a common market that unites the national markets of the Member States and on which all goods and services can be offered and sold on the same conditions as on an internal market and to which all Union citizens have the same, free access"* – see K. Borchardt, *The ABC of European Union Law* (Luxembourg: Publications Office of the European Union, 2010), p. 33.

[7] Explaining reverse discrimination as emerging from the EU's activities in furthering the internal market, see A. Tryfonidou, *supra* n. 3, pp. 14-18.

[8] The harmonisation of legislation concerning indirect taxation is expressly foreseen in article 113 TFEU.

[9] Nor is it included within the scope of article 114 TFEU, the general provision on the approximation of the Laws of the Member States.

Member States when those are considered to directly affect the establishment or functioning of the internal market[10].

Nonetheless, any possibility of harmonization as a mean to secure equal treatment builds, of course, on the TFEU's own provisions destined to forbid discrimination within the EU. Among these article 18 TFEU deserves to be highlighted as the general provision forbidding discrimination on the grounds of nationality:

> Within the scope of application of the Treaties, and without prejudice to any special provision contained therein, any discrimination on grounds of nationality shall be prohibited[11]

At first glance, one is tempted to read article 18 TFEU as prohibiting any discrimination on grounds of nationality, including reverse discrimination by a Member State of its own nationals. Under closer scrutiny, however, one realises that the prohibition is limited by the two opening segments: "within the scope of application of the Treaties" and "without prejudice to any special provision contained therein"[12].

The latter means that article 18 TFEU will only apply in circumstances where other more specific provisions do not. Notably, since the fundamental freedoms provisions themselves also prohibit discrimination, the general provision forbidding discrimination on the grounds of nationality will not apply to situations comprised within their field of application. As duly noted by Ghosh:

> The Court has made it clear that since the substantive provisions which confer the freedoms themselves prohibit discrimination, article 12 [article 18 TFEU] cannot apply to any circumstance to which any of those provisions apply. This is the case in relation to all of the freedoms […]. So article 43 [article 49 TFEU] occupies the "entire field" of prohibited discriminatory treatment in relation to the establishment of self-employed persons. It is not that article 12 [article 18 TFEU] supplements the application of article 43 [article 49 TFEU]. Article 43 [article 49 TFEU] enacts article 12 [article 18 TFEU] in the entirety of its scope in relation to self-employed persons. Article 12 [article 18 TFEU] thus has no residual application to the "field" in which article 43 [article 49 TFEU] applies. […] Neither can article 12 [article 18 TFEU] apply in circumstances involving goods, capital or payments within the scope of articles 28, 29 or 56 respectively [articles 34, 35 and 63 TFEU respectively], since […] all of the freedoms must share an identical jurisprudence by reason of having a common basis, in article 3.1.c, of the Treaty [repealed but maintained in substance by article 26 TFEU][13]

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[10] In theory, such harmonization could also be achieved through the procedure foreseen in article 116 TFEU, on the basis that lack of harmonization distorts competition in the internal market and needs to be eliminated. Historically, however, such procedure has never been chosen as a mean to achieve harmonization in direct taxation. Another alternative yet to be pursued to (even if only partially) harmonize direct tax rules would be the enhanced cooperation possibility foreseen in article 20 TEU. On the subject of tax harmonization in the EU see A. Schrauwen, "Sources of EU Law for Integration in Taxation", in *Traditional and Alternative Routes to European Tax Integration*, ed. D. Weber (Amsterdam: IBFD, 2010), pp. 15-28.

[11] The second paragraph of article 18 TFEU further states that *"the European Parliament and the Council, acting in accordance with the ordinary legislative procedure, may adopt rules designed to prohibit such discrimination"*. This however cannot be taken to imply that the first paragraph is deprived of direct effect – on this particular point, see A. Arnull, *The European Union and its Court of Justice* (Oxford: Oxford University Press, 2006), p. 502.

[12] On such limits see G. Davies, *European Union Internal Market Law* (Abingdon: Routledge-Cavendish, 2003), pp. 118-119.

[13] J. Ghosh, *Principle of the Internal Market and Direct Taxation* (Oxford: Key Haven, 2007), pp. 66-67.

In fact, the wording of the fundamental freedoms provisions leaves little doubt that these too are nationality non-discrimination clauses[14]. Accordingly, one may not fall back to article 18 TFEU to do away with discrimination in matters addressed by the fundamental freedoms provisions whenever such discrimination is not precluded by these.

As to the first segment of article 18 TFEU, it too narrows the area of application of the general non-discrimination provision, limiting its applicability to the scope of application of the Treaties. This seems *prima facie* quite redundant. Logically, one would say, the applicability of any treaty provision cannot exceed that of the treaty of which it is a part of[15]. Be that as it may, such reference unequivocally demands acknowledgment of the Treaties' scope when assessing the scope of application of article 18 TFEU. As a consequence, as remarked by d'Oliveira:

> Within the framework of Community law, a State may not treat its own citizens worse than citizens of other Member States (and vice-versa), but otherwise such discrimination is permissible. A Member State may treat citizens of third countries worse than those of Member States: outside the Community legal system, even citizens of Member States may be discriminated against, or at any rate the Community legal system as such does not preclude it. Other treaties or constitutional bans on discrimination may of course lay down limitations in this respect. It follows that a distinction should be drawn between "situations under Community law" and other situations, in particular the wholly external situations and those that fall entirely under the law of one of the Member States ("internal cases")[16]

Delimitation of the scope of application of the Treaties is a task to a large extent left to the CJEU[17]. In performing such a task, the CJEU has developed the doctrine of "purely internal situations" to label those circumstances that remain outside the scope of EU Law. The first time such doctrine was applied by the CJEU was in the *Saunders* case, on the free movement of workers, where it stated that:

> The provisions of the Treaty on freedom of movement for workers cannot […] be applied to situations which are wholly internal to a Member State, in other words, where there is no factor connecting them to any of the situations envisaged by Community Law[18]

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[14] Only article 63 TFEU on the free movement of capital and payments omits any reference to nationality, prohibiting all restrictions on such movement between Member States (and between Member States and third countries). Nevertheless such prohibition also comprises discrimination on grounds of nationality – CJEU, 14 Oct. 1999, Case C-439/97, *Sandoz GmbH v Finanzlandesdirektion für Wien, Niederösterreich und Burgenland*, ("*Sandoz*"), [1999] ECR I-7041.

[15] Notwithstanding, such an express statement somehow clarifies that, even if the EU may be seen as an ever evolving entity, with an expanding scope, the general non-discrimination provision is not intended to broaden such scope but simply to apply within the orbit of the Treaties otherwise outlined.

[16] H.U.J. d'Oliveira, "Is Reverse discrimination still permissible under the Single European Act?", in *Forty years on: The Evolution of Postwar Private International Law in Europe* (Deventer: Kluwer, 1990), p. 72.

[17] As remarked by A. Tryfonidou: *"Although in the EC, as in other supranational organisations, the need has always existed to accurately define the boundaries of the scope of each level of governance (i.e. national and supranational), a definite line between the two levels of governance has never been drawn by the drafters of the various Treaties. Rather, quite surprisingly, this delicate and politically charged issue was left to the Court of Justice which, through its case-law, would, inter alia, have to specify the limits to the ambit of the various Treaty Articles"* – see A. Tryfonidou, "The Outer Limits of Article 28 EC: Purely Internal Situations and the Development of the Court's Approach Through the Years", in *Social Science Research Network* (http://ssrn.com/abstract=1029248), p. 2.

[18] CJEU, 28 Mar. 1979, Case 175/78, *R v Saunders*, ("*Saunders*"), [1979] ECR 1129, paragraph 11.

Thus, according to the CJEU, for a situation to fall within the scope of application of the Treaties it must present a connection with the relevant provisions of EU Law potentially in play. In other words:

> The notion of purely internal situations varies depending on the area of EC Law which is invoked. A given situation may or may not come under EC Law depending on the rule applicable and on the degree of legal integration in that area[19]

The observation that the scope of EU Law, and therefore the span of application of both the fundamental freedoms provisions and of the general non-discrimination provision, varies as a function of the degree of integration in the particular field of law engaged fits elegantly with the realization of the EU as both a reality created by and a community based on law[20].

III – THE AREA OF DIRECT TAXATION

As previously mentioned, the direct taxation field is not, to say the least, one of great harmonization. Nor one the Treaties address significantly. In other words, when it comes to direct taxation the scope of application of the Treaties is relatively narrow. This means that the number of purely internal situations to be found in direct tax matters will almost certainly be larger than in other, more advanced, areas of European integration[21]. But the question still stands: are situations of reverse discrimination in direct taxation to be found within or outside the scope of EU Law?

According to Garcia, direct taxation, given the lack of positive harmonization, is in dire need of negative integration by the CJEU:

> The field of direct taxation is, in the absence of secondary law, asking desperately for negative integration. It has been recognized that the Court can neither take any political decision nor allocate taxing powers between Member States; therefore, cases of for example double taxation, arising due to disparities are outside the scope of Community law. However […] reverse discrimination is not a consequence of these matters alien to EC Law. Conversely, they are problems created by a single jurisdiction that national measure is less advantageous to citizens of that State than to foreigners. The Court cannot harmonize disparities, true; but it can perfectly solve the problems of inequality among citizens of the Union created by the application of a national rule in an internal situation[22]

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[19] M. P. Maduro, "The Scope of European Remedies: the case of Purely Internal Situations and Reverse Discrimination?", in *The Future of European Remedies*, eds. C. Kilpatrick, T. Novitz, P. Skidmore (Oxford: Hart Publishing, 2000), p. 120.

[20] Quoting K. Borchardt (*supra* n. 6, p. 79), *"this is what is entirely new about the EU, and what distinguishes it from earlier attempts to unite Europe. It works not by means of force or subjugation but simply by means of law.* […] *However, the EU is not merely a creation of law but also pursues its objectives purely by means of law. It is a community based on law"*. Also advocating a juridical approach to the task of defining the scope of EU Law, over a geographical approach, d'Oliveira (*supra* n. 16, p. 75) remarks: *"in defining Community cases it is important to determine the object and scope of Community rules.* […] *Whether or not the Community legal system is brought in cannot depend, at any rate not exclusively, on some sort of catalogue of contacts or factual points of reference. It depends partly, perhaps even predominantly, on the very teleology and dynamics of the Community legal system"*.

[21] Clear examples of such areas of (more) advanced integration are Value-Added Tax and Custom Duties.

[22] D. Garcia, *supra* n. 3, p. 181.

Hence, under such view, reverse discrimination is presented, not as the result of political decisions or of the allocation of taxing powers between Member States, but simply as the product of national rules applied by Member States in such a way that is detrimental to the equality among EU citizens. The CJEU would then be quite capable of deeming the application of such national rules as in breach of the TFEU, notably of the principle of equality underlying both the general non-discrimination and the fundamental freedoms provisions.

In our opinion, however, the problem is not that simple nor is the answer that straightforward. First of all, it must be said that since the problem of reverse discrimination arises from the application of national legal rules enacted by Member States, it is indeed the result of political decisions. Even if, more often that not, reverse discrimination may be the unplanned or unwanted outcome of such decisions. Secondly, the capability of the CJEU to do away with reverse discrimination is not a matter at the Court's discretion. The CJEU's function is to interpret and apply EU Law and therefore it is either bound to forbid it or required to allow it.

Therefore, the focus must instead be placed on EU Law itself. With that in mind, addressing the subject of direct taxation one inevitably needs to recall the CJEU's mantra on the division of competences between the EU and the Member States regarding the subject:

> Although, as Community law stands at present, direct taxation does not as such fall within the purview of the Community, the powers retained by the Member States must nevertheless be exercised consistently with Community law[23]

Basing itself on such assertion, the CJEU has developed a significant body of case law on direct taxation, trying to ascertain precisely what it means for Member States to exercise their retained taxing powers in a way consistent with EU Law. In doing so, the CJEU has stricken down Member States' tax rules due to them being discriminatory on the grounds of nationality. As a preliminary observation to this statement one should remark that most national tax systems are designed on the basis of residency and not of nationality. This entails that national tax provisions directly discriminating on the grounds of nationality are atypical.

Nevertheless, according to settled case law by the CJEU, non-discrimination provisions prohibit not only direct discrimination but also indirect discrimination[24]. This occurs by application of any other criterion of differentiation leading to the same result. Addressing the differentiation between residents and non-residents, the CJEU as ruled that:

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[23] CJEU, 14 Feb. 1995, Case C-279/93, *Finanzamt Köln-Altstadt v Roland Schumacker*, ("*Schumacker*"), [1995] ECR I-225, paragraph 21. A similar phrase heads virtually all of the Court's findings in the CJEU's case law on direct-tax matters.

[24] CJEU, 12 Feb. 1974, Case 152/73, *Giovanni Maria Sotgiu v Deutsche Bundespost*, ("*Sotgiu*"), [1974] ECR 153.

> Even though the criterion of permanent residence in the national territory […] applies irrespective of the nationality of the taxpayer concerned, there is a risk that it will work in particular against taxpayers who are nationals of other Member States[25]

This means that a detrimental treatment afforded to non-residents by the tax system of a Member State may amount to indirect discrimination on the grounds of nationality, thus breaching the non-discrimination provisions of the TFEU if residents and non-residents are deemed to be in comparable circumstances[26].

Accordingly, even if they challenge the tax treatment of non-residents by comparison to that of residents, most of the direct tax cases brought to the CJEU deal with non-nationals pointing to a more favourable tax treatment of nationals and demanding equal benefit[27]. Other cases involve nationals complaining of suffering less advantageous tax treatment by their own Member State because of having exercised EU freedoms instead of confining their actions to their home territory[28].

It is this second type of cases that particularly merits attention within the present study. In them, the CJEU has clarified that the non-discrimination provisions also apply to Member States in respect to their own nationals. The approach followed by the CJEU is to compare the situation of the person exercising the EU freedom to someone refraining to do so and for that reason enjoying a better tax treatment.

Examining the reasoning of the CJEU in this type of cases, some Authors submit that it is totally different from the reasoning followed in applying the principle of equality underlying the non-discrimination provisions:

> The concept of prohibition of restriction is different from the concept on non-discrimination […]. The issue here is not one of classical discrimination, that makes a distinction between different categories of taxpayers. It is about obstacles that constitute handicaps for cross-border trade[29]

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[25] CJEU, 8 May 1990, Case C-175/88, *Klaus Biehl v Administration des Contributions du Grand-Duché de Luxembourg*, ("*Biehl*"), [1990] ECR I-1779, paragraph 14.

[26] Even if under such approach the CJEU typically ends up comparing the tax treatment afforded to non-residents with that of residents, one should not lose sight that it is nonetheless a comparison made while ascertaining whether any (indirect) discrimination on the grounds of nationality exists. Therefore, unlike others (D. Garcia, *supra* n. 3, p. 184), this Author fails to see in the CJEU's approach any contradiction or inconsistency dictating that the Court should abandon comparisons on the ground of nationality altogether and simply compare on the basis of residence in order to abide by the principle of equality and do away with, *inter alia*, reverse discrimination.

[27] *E.g.*: CJEU, 28 Jan. 1986, Case 270/83, *Commission of the European Communities v French Republic*, ("*Avoir Fiscal*"), [1986] ECR 273; CJEU, 14 Feb. 1995, Case C-279/93, *Schumacker*; CJEU, 12 Jun. 2003, Case C-234/01, *Arnoud Gerritse v Finanzamt Neukölln-Nord,* ("*Gerritse*"), [2003] ECR I-5933; and CJEU, 19 Jan. 2006, Case C-265/04, *Margaretha Bouanich v Skatterverket,* ("*Bouanich*"), [2006] ECR I-923.

[28] *E.g.*: CJEU, 26 Oct. 1999, Case C-294/97, *Eurowings Luftverkehrs AG v Finanzamt Dortmund-Unna*, ("*Eurowings*"), [1999] ECR 7447; CJEU, 12 Dec. 2002, Case C-385/00, *F. W. L. de Groot v Staatssecretaris van Financiën*, ("*De Groot*"), [2002] ECR I-11819; CJEU, 7 Sep. 2004, Case C-319/02, *Petri Manninen*, ("*Manninen*"), [2006] ECR I-7477; and CJEU, 13 Dec. 2005, Case C-446/03, *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes)*, ("*Marks & Spencer*"), [2005] ECR I-10837.

[29] F. Vanistendael "The compatibility of the Basic Economic Freedoms with the Sovereign National Tax Systems of the Member States", *EC Tax Review* 2003, no. 3, p. 137.

However, under closer examination one concludes that the reasoning of the Court, even when considering whether an unlawful restriction is in place, does not cease to be one of assessing discrimination under the principle of national treatment test, even if regarding the Member State's own nationals[30]. In the CJEU's own words:

> Member States must […] respect the principle of national treatment of nationals of other Member States and of their own nationals who exercise the freedoms guaranteed by the Treaty[31]

For the purpose of our analysis, the relevance of this extension of the principle of national treatment to nationals of the Member State concerned is that it entails that some instances of reverse discrimination in direct tax matters have already been considered contrary to EU Law.

In fact, it follows from such case law that Member States are prohibited of deterring their own nationals from taking advantage of their EU rights. This means that, in order to fully comply with their Treaty obligations, Member States not only need to acknowledge the fundamental freedoms of nationals from other Member States, but are also obliged to respect the EU rights of their own nationals[32].

Thus, in direct tax matters, an area in which discrimination by a Member State of its own nationals is prohibited by EU Law does exist. And to that extent, any reverse discrimination of a Member State against its nationals occurring within that area will also be prohibited[33].

It must notwithstanding be borne in mind that such reverse discrimination prohibition will only exist when EU Law rights of the concerned Member State nationals are jeopardized. Other instances of reverse discrimination will fall outside the scope of the Treaties. Moreover, the chances of instances of reverse discrimination occurring are undoubtedly increased by the fact that, under EU Law, non-

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[30] See T. O'Shea, *EU Tax Law and Double Tax Conventions* (London: Avoir Fiscal, 2008), pp. 46-48.

[31] CJEU, 12 Dec. 2002, Case C-385/00, *De Groot,* paragraph 94.

[32] As synthesized by the CJEU, *"it is settled law that, although the provisions of the Treaty relating to freedom of establishment cannot be applied to situations which are purely internal to a Member State, Article 52* [article 49 TFEU] *nevertheless cannot be interpreted in such a way as to exclude a given Member State' s own nationals from the benefit of Community law where by reason of their conduct they are, with regard to their Member State of origin, in a situation which may be regarded as equivalent to that of any other person enjoying the rights and liberties guaranteed by the Treaty"* – CJEU, 27 Jun. 1996, Case C-107/94, *P.H. Asscher v Staatssecretaris van Financiën*, ("*Asscher*"), [1996] ECR I-3089, paragraph 32.

[33] To better illustrate this point, one may refer to CJEU, 26 Oct. 2006, Case C-345/05, *Commission of the European Communities v Portuguese Republic*, ("*Commission v Portugal – Housing Aid*"), [2006] ECR I-10633. At stake was a Member State's regime exempting capital gains derived from the sale of immoveable property intended for the taxpayer's residence, on the condition that the sale proceeds were reinvested in real estate for the same purpose located in that Member State's territory. The Court found that regime breached the freedoms addressing movement of individuals, since it was liable to deter resident taxpayers from transferring their residence abroad, hence impairing the exercise of EU rights. The fact that Member States are obliged to acknowledge the EU rights of their own nationals entails that the regime at stake could not be made compliant with EU Law by simply extending the exemption to reinvestment abroad in case of nationals of other Member States. Necessary extension to nationals of the Member State concerned intending to transfer their residence to other Member States unequivocally shows some instances of reverse discrimination are in fact prohibited.

discrimination against nationals of another Member State actually means "no less favourable treatment", and not "equal treatment". Different, but no less favourable treatment is permissible and national treatment of those exercising EU rights is held by the CJEU to be a minimum standard, not a goal[34].

Put differently, at least in the field of direct taxation, Member States are still at liberty to discriminate against their own nationals provided that such discrimination does not hinge on the exercise of EU Law rights and to the detriment of those exercising said rights[35].

In particular, if it so desires, a Member State may exercise it's retained taxing powers specifically targeting its own nationals, as long as the tax provisions at stake do not impair their EU rights. Accordingly, the CJEU has ruled that:

> National legislation […] which provides that the estate of a national of a Member State who dies within 10 years of ceasing to reside in that Member State is to be taxed as if that national had continued to reside in that Member State, while providing for relief in respect of the taxes levied in the State to which the deceased transferred his residence, does not constitute a restriction on the movement of capital. […] By enacting identical taxation provisions for the estates of nationals who have transferred their residence abroad and of those who have remained in the Member State concerned, such legislation cannot discourage the former from making investments in that Member State from another State nor the latter from doing so in another Member State from the Member State concerned […]. As regards the differences in treatment between residents who are nationals of the Member State concerned and those who are nationals of other Member States resulting from national legislation such as that in question in the main proceedings, it must be observed that such distinctions, for the purposes of allocating powers of taxation, cannot be regarded as constituting discrimination prohibited by Article 73b of the Treaty [article 63 TFEU]. They flow, in the absence of any unifying or harmonising measures adopted in the Community context, from the Member States' power to define, by treaty or unilaterally, the criteria for allocating their powers of taxation[36]

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[34] A clear example of this may be seen in CJEU, 19 Jan. 2006, Case C-265/04, *Bouanich*, [2006] ECR I-923, in which the Court held that a more beneficial treatment afforded to a non-resident under a Double Tax Treaty could act to remove in practice the restrictive effect of a domestic tax regime that would otherwise be incompatible with the fundamental freedoms.

[35] Contrary to what some believe this does not mean that *"citizens of a Member State* […] *who decide to stay in their State of nationality lose the rights granted by the Treaty to citizens of the Union"* (D. Garcia, *supra* n. 3, p. 184). EU citizens circumstantially not exercising EU rights are not deprived of them. To put it bluntly: the fact someone is staying still does not imply the absence of a right to move.

[36] CJEU, 23 Feb. 2006, Case C-513/03, *Heirs of M.E.A. van Hilten-van der Heijden v Inspecteur van de Belastingdienst / Particulieren / Ondernemingen buitenland te Heerlen*, ("*Van Hilten*"), [2006] ECR I-1957, paragraphs 45-7. Although this case clearly shows that nationality may be accepted as a criterion delineating tax jurisdiction, it should be borne in mind that the facts in the main proceedings dictated an analysis by the CJEU limited to the free movement of capital from a third country to a Member State. A careful reading of the Court's reasoning – in particular paragraphs 49-50 – suggests that such conclusion may not have been so clear-cut had the situation involve movement between two Member States, thus triggering an analysis under the exercise of freedom of establishment or of the right to move and reside freely. In fact, from a theoretical point of view, applying a nationality criterion as a basis of asserting tax jurisdiction would most likely entail juridical double taxation for nationals leaving their Member State of origin to establish themselves in another Member State. In principle, such double taxation would be taken as simply deriving from the exercise in parallel of the tax sovereignty of two Member States, not amounting to a breach of the fundamental freedoms – CJEU, 14 Nov. 2006, Case C-513/04, *Mark Kerckhaert and Bernadette Morres v Belgium*, ("*Kerckhaert-Morres*"), [2006] ECR I-10967, paragraph 20; CJEU, 16 Jul. 2009, Case C-128/08, *Jacques Damseaux v État belge*, ("*Damseaux*"), [2009] ECR I-06823, paragraph 27. Nonetheless, it is unclear whether nationality as a criterion for taxation is to be found acceptable under EU Law in all circumstances. Even if the CJEU has accepted disparities resulting from the convergence of tax sovereignties, thus paying respect to the Member States' retention of taxing powers, it consistently sought to stress the reasonability of whichever regime was under analysis, typically by reference to standarts of international tax practice – CJEU, 23 Feb. 2006, Case C-513/03, *Van Hilten*, [2006] ECR I-1957, paragraph 48; CJEU, 14 Nov. 2006, Case C-513/04, "*Kerckhaert-Morres*", [2006] ECR I-10967, paragraph 23; CJEU, 16 Jul. 2009, Case C-128/08, "*Damseaux*", [2009] ECR I-06823, paragraph 30. This seems to entail that an unreasonable use of nationality as a criterion for taxation – *e.g.*

It is important to note that this liberty kept by the Member States is consistent with what was stated above regarding the scope of the Treaties: the exercise by a Member State of its retained taxing powers in the field of direct taxation with respect to its own nationals, in the absence of harmonization, and provided that said exercise does not hinder such nationals' EU Law rights, constitutes purely internal situations not precluded by EU Law.

Contrary to what some believe[37], this basic assertion is not fundamentally changed by the introduction of the status of EU citizenship, established by article 20 TFEU and granted to every national of a Member State as an addition to national citizenship. According to article 20 TFEU:

> Citizens of the Union shall enjoy the rights and be subject to the duties provided for in the Treaties. They shall have, inter alia: […] the right to move and reside freely within the territory of the Member States […]. These rights shall be exercised in accordance with the conditions and limits defined by the Treaties and by the measures adopted thereunder

The most significant right attached to the EU citizenship status is without question the right to move and reside freely within the territory of the Member States[38]. This has in fact extended Treaty rights to those not economically active that, for that reason, were previously unable to benefit from the fundamental freedom provisions. As one would expect, such extension has also proven relevant to the field of direct taxation[39].

This surfacing of a group of people enjoying EU rights other than those arising from the four fundamental freedoms, has raised questions as to the exact consequences of the interaction of EU citizenship with the general non-discrimination clause of article 18 TFEU. In short, some submit that the two provisions combined dictate an overall prohibition of reverse discrimination within the EU[40]. However, as noted by the CJEU, this extension of the Treaties' scope *ratione personae* did not alter their scope *ratione materiae*:

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not in line with international tax practice, such as to the detriment of nationals of other Member States – could in fact be found incompatible with EU Law. Specifically in what concerns reverse discrimination on grounds of nationality and the possible adoption of nationality as a criterion for taxation, a reasonable exercise of retained taxing powers by a Member State will at least imply non-resident nationals and resident nationals being afforded similar treatment, notably regarding relief of international double taxation.

[37] See D. Garcia, *supra* n. 3, pp. 184-188.

[38] Detailed in article 21 TFEU. This provision further specifies that said right is *"subject to the limitations and conditions laid down in the Treaties and by the measures adopted to give them effect"*. On the status of EU citizenship, see G. Davies, *supra* n. 12, pp. 66-73.

[39] As acknowledged by the CJEU, which has paired the right to move and reside freely foreseen in article 21 TFEU to the free-movement of workers and freedom of establishment provisions in protecting nationals against a tax provision deterring them from leaving their country of origin to other Member States – CJEU, 26 Oct. 2006, Case C-345/05, *Commission v Portugal – Housing Aid*, [2006] ECR I-10633.

[40] See D. Garcia, *supra* n. 3, p. 186.

> It must be noted that citizenship of the Union, established by Article 8 of the EC Treaty [article 20 TFEU], is not intended to extend the scope ratione materiae of the Treaty also to internal situations which have no link with Community law[41]

The fact that the introduction of EU citizenship is not aimed at broadening the material scope of the Treaties makes it impossible for it to serve the goal of attaining an overall prohibition of reverse discrimination. It suffices to recall that application of article 18 TFEU is expressly limited to the scope of the Treaties and therefore not intended to expand it[42].

Therefore, with relevance to the matter of reverse discrimination and direct taxation, the practical consequence of EU citizenship is simply that of prohibiting a Member State to reversely discriminate its nationals in similar fashion as reverse discrimination is prohibited in the context of the fundamental freedoms. Member States need to respect EU citizenship rights of both nationals and non-nationals and therefore are inhibited from any discrimination against nationals that hinders such rights, notably the right to move and reside freely. Only to that extent can one say EU citizenship further compresses the range of purely internal situations.

IV – CONCLUSION

It follows from the above-stated that the CJEU doctrine of "purely internal situations" is the inevitable result of the limited scope of application of the Treaties and of the coexistence between EU Law and the Member States' legal orders. However, to say reverse discrimination has its origin in it is not an accurate statement. Moreover, even in fields such as direct taxation where the scope of EU Law is relatively small, some instances of reverse discrimination are in fact prohibited, should Member States try to hinder their nationals' exercise of EU rights[43].

One sympathises with those demanding reverse discrimination to be eradicated and understands the attractiveness of having the CJEU as an ally in such struggle. Nevertheless, it should come as no surprise that when EU Law is not at stake EU protection is equally absent. Accordingly, one should not overlook that the inherent injustice reverse discrimination entails resides in the Member States' own legal orders. It is there, therefore, that it should be properly dealt with.

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[41] CJEU, 5 Jun. 1997, Joined Cases C-64/96 and C-65/96, *Land Nordrhein-Westfalen v Kari Uecker and Vera Jacquet v Land Nordrhein-Westfalen*, ("*Uecker and Jacquet*"), [1997] ECR I-3171, paragraph 23.

[42] For similar reasons, a general prohibition of reverse discrimination within the EU also cannot be derived from the Charter of Fundamental Rights of the European Union ("CFREU") or from the accession of the EU to the European Convention for the Protection of Human Rights and Fundamental Freedoms ("ECHR"). In fact, both the CFREU and article 6 TEU (foreseeing accession to the ECHR) explicitly state that they are not to be construed as expanding the Treaties' scope. One must therefore once again differ from D. Garcia (D. Garcia, *supra* n. 3, pp. 186-188).

[43] This has actually led some to redefine reverse discrimination as *"discrimination based on the ground of non-contribution to the internal market"* – see A. Tryfonidou, *supra* n. 1, p. 19. Be that as it may, instead of redefining concepts to safe keep conclusions one favours following the opposite route.