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Case C-593/14


Synopsis

The freedom of establishment precludes legislation of a Member State, which allows a resident company a tax exemption for interest paid by a resident subsidiary, in so far as that subsidiary is not entitled to a tax deduction for the corresponding interest expenditure by reason of the rules limiting the deduction of interest paid in cases of thin capitalization, but which excludes the exemption that would result from the application of its own thin capitalization legislation in the case where the subsidiary is resident in another Member State.

Facts

Damixa ApS (Danish Parent) is a Danish parent company holding all the shares in subsidiary Damixa Armaturen GmbH resident in Germany (German Subsidiary). Danish Parent had granted a loan to German Subsidiary in respect of which it received interest. German Subsidiary was not entitled to deduct the interest paid to Danish Parent due to German thin capitalization rules. The Danish tax authorities took the view that the interest received from German Subsidiary was taxable income for Danish Parent, although it would have been tax exempt if received from a subsidiary resident in Denmark. Danish Parent appealed the decision arguing that disallowing the exemption was against the freedom of establishment as the exemption was denied only because the interest was received from a subsidiary resident in another Member State. The Danish High Court requested a preliminary ruling on the issue from the ECJ.

Legal background and issue

Under Danish law, if the interest is not deductible for the payer due to thin capitalization rules, the interest income is tax exempt for its recipient. The Danish tax authorities took the view that this provision only applies to companies resident in Denmark.
The issue was whether the freedom of establishment precludes legislation which grants a resident company a tax exemption in respect of interest paid by a resident subsidiary, in so far as that subsidiary is not entitled to a tax deduction for the corresponding interest expenditure due to thin capitalization rules, but does not grant such an exemption where the subsidiary is resident in another Member State.

**Decision**

**Scope**
The ECJ examined the case based on the freedom of establishment.

**Discrimination/restriction**
Providing a tax exemption to a resident company for interest paid by a resident subsidiary in so far as that subsidiary is not entitled to a tax deduction for the corresponding interest by national rules limiting interest deduction in cases of thin capitalization constitutes a tax advantage. Denying such an advantage for a resident company in relation to interest paid to that company by a subsidiary resident in another Member State is liable to render less attractive the exercise by that parent company of its freedom of establishment by deterring it from setting up subsidiaries in other Member States.

Such a difference in treatment is permissible only if it relates to situations which are not objectively comparable or if it is justified by an overriding reason in the public interest. The situation in which a resident parent company has granted a loan to a resident subsidiary that is subject to thin capitalization rules (i.e. internal situation) and the situation in which a resident parent company has granted a loan to a non-resident subsidiary that is subject to thin capitalization rules in the Member State in which it is resident for tax purposes (i.e. cross-border situation) are objectively comparable. In each of those situations, the interest income received by the parent company is liable to be subject to economic double taxation or to a series of charges, which is what the legislation at issue seeks to avoid.

**Justifications**

(i) **Balanced allocation of taxing powers** – The legislation in question ensures the balanced allocation of taxing powers between Member States by limiting the tax exemption solely to interest paid by a resident subsidiary. If the tax exemption would be allowed in respect of interest paid by a non-resident subsidiary where the subsidiary is not entitled to deduct the interest expenditure under the thin capitalization rules of that other Member State, the Member State in which the parent company is resident would give away its right to tax the interest income received by the parent company depending on the thin capitalization rules adopted by the Member State of residence of the subsidiary. This is the objective the legislation at issue seeks to avoid.

In order to be so justified, such a difference must be appropriate to attain the objective pursued and must not go beyond what is necessary to achieve that objective (proportionality). The national legislation in question goes beyond what is necessary to achieve the objective of the national legislation. A Member State is not, however, required to draw up its tax rules on the basis of those in another Member State in order to remove disparities arising from
national tax rules. Hence, a less restrictive measure in line with the balanced allocation of taxing powers would be to provide a tax exemption to the parent company for interest paid by the subsidiary resident in another Member State up to the amount that the subsidiary was not entitled to deduct under the thin capitalization rules of the residence state of the parent company.

(ii) **Prevention of tax avoidance** – The ECJ rejected this justification as the legislation at issue does not specifically aim at preventing wholly artificial arrangements but generally excludes all resident companies that have granted, irrespective of the reason, a loan to a thinly capitalized subsidiary resident in another Member State. In the case at issue, it was also clear that the loan Danish Parent granted to German Subsidiary was to finance the latter which was in major financial difficulties. Therefore, the loan arrangement did not constitute a wholly artificial arrangement entered into only for tax reasons.

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**Case C-18/15**  
**Brisal – Auto Estradas do Litoral S.A., KBC Finance Ireland v. Fazenda Pública**

- **Decision date:** 13 July 2016  
- **Procedure type:** Preliminary ruling  
- **AG opinion:** Kokott, 17 March 2016  
- **Justifications:** Balanced allocation of taxing powers, double deduction, effective collection of taxes  
- **Decision type:** Judgment  
- **Legal basis:** Art. 49 EC Treaty, Art. 56 TFEU (Freedom to provide services)  
- **Host State/Home State:** Host state  
- **Keywords:** Corporate income tax, interest, administrative burden, business expenses, cross-border services, loan, tax at source, tax treaty, withholding tax, offsetting other advantages  
- **Authentic language:** Portuguese

**Synopsis**

National legislation subjecting interest paid to a non-resident financial institution to a withholding tax on a gross basis whereas interest paid to a resident financial institution is not subject to such tax and is able to deduct business expenses, is contrary to the freedom to provide services.

**Facts**

The taxpayer, Portuguese resident company Brisal – Auto Estradas do Litoral S.A. (Brisal) and the Irish bank KBC Finance Ireland (KBC) were partners under a financing contract. Within that framework, Brisal paid interest to KBC in the years 2005 to 2007. Brisal withheld the tax from those payments and remitted it to the Portuguese tax authorities on behalf of KBC.
Brisal and KBC challenged the application of the withholding tax on interest paid to non-resident financial institutions as they took the view that the relevant national rules discriminated non-residents. The Supreme Administrative Court referred the case to the ECJ.

**Legal background and issue**

Under Portuguese law, interest income paid to a non-resident legal entity (such as a non-resident financial institution) is subject to a 20% withholding tax on a gross basis, unless there is a tax treaty providing a lower withholding tax rate, whereas interest paid to a resident financial institution is taxed at 25% on net basis, without being subject to withholding tax.

The issues were whether:

(i) the national legislation in question was compatible with the freedom to provide services when it taxed a non-resident financial institution by means of withholding tax on interest income received from Portugal whereas the income received by resident financial institutions is not subject to such tax;

(ii) the fact that non-residents, unlike residents, could not deduct business expenses directly related to the financial activity in question constituted a restriction, and, if so, whether such a restriction could be justified; and

(iii) the average interest rates could be regarded as constituting business expenses directly related to the financial activity in question.

**Decision**

**Scope**

The Court examined the case based on the freedom to provide services.

**Discrimination/Restriction**

In respect of the first issue, the Court held that the freedom to provide services does not preclude the application of withholding tax, as a method of taxation to non-resident service providers when resident service providers are not subject to such tax provided that the application to the non-resident financial institutions of the withholding tax is justified by an overriding reason in the general interest and does not go beyond what is necessary to attain the objective pursued.

Regarding the second issue, under settled case law of the Court, resident service providers and non-resident service providers are in a comparable situation in relation to the deduction of business expenses. Hence, the freedom to provide services precludes a national legislation which generally takes into account gross income when taxing non-residents, without deducting business expenses, whereas residents are taxed on their net income, after deduction of those expenses.

The third issue on how to determine the business expenses directly related to the interest income arising from a financial loan arrangement, the Court referred to its previous case law under which it has been established that if a Member State grants residents the opportunity to deduct such expenses it may not preclude the deduction of those same expenses for non-residents. Business expenses directly
related to the income received in the Member State in which the activity is pursued must be understood as expenses occasioned by the activity in question, and therefore necessary for pursuing that activity. It is rather easy to both establish the link with the loan granted (i.e. the service provided) and to prove the actual business expenses related to it. For some expenses, such as financing costs and general expenses of the financial institution, it may prove to be more difficult to establish a direct link with a given loan or the actual amount involved although such expenses are, in principle, necessary to the pursuit of that activity. Nevertheless, the mere fact that that evidence is more difficult to provide cannot authorize a Member State to deny categorically to non-residents, a deduction which it grants to residents due to the fact that it cannot *a priori* be ruled out that a non-resident is able to provide relevant evidence enabling the tax authorities of the Member State of taxation to ascertain, clearly and precisely, the nature and genuineness of the business expenses in respect of which deduction is sought. The Court concluded that it is for the referring court to determine which of the expenses claimed by KBC may be regarded as business expenses directly related to the financial activity in question and secondly, what is the fraction of the general expenses which may be regarded as directly related to that activity. The Court, however added that unless national legislation authorizes resident financial institutions to use, in the calculation of the financing costs incurred, interest rates such as those mentioned by the referring court, those rates cannot be taken into account as they constitute only average rates charged in the context of interbank financing and do not correspond to the financing costs actually incurred. Furthermore, the loan at issue was not financed exclusively by funds borrowed from KBC’s parent company and other banks, but it was also financed through funds deposited by KBC’s clients.

**Justifications**

(i) *Balanced allocation of taxing rights.* The Court, in line with the Advocate General’s opinion, rejected this justification as there is nothing in the case at hand which could explain in what way the allocation of taxing rights requires that a non-resident financial institution must be treated less favourably than resident financial institutions with regard to the deduction of business expenses directly related to their taxable income in that Member State.

(ii) *Prevention of double deduction of business expenses.* The Court rejected also this justification due to the fact that Portugal had not clarified how the risk of double deduction of such expenses could not be prevented by the implementation of the Directive 77/799.

(iii) *Ensuring the effective collection of tax.* The effective collection of tax can constitute an overriding reason of public interest but the restriction must still be applied in such a way that the aim pursued is achieved but does not go beyond what is necessary for that purpose. The Court pointed out that the administrative burden for the national tax authorities due to the fact that a deduction of business expenses is allowed is caused not just for allowing resident financial institutions to deduct such expenses but is the same for allowing it for non-resident financial institutions. In respect of the administrative burden for the recipient of the service seeking to deduct, the Court emphasized that such burden exists only in a system which provides that
that deduction must be made before withholding tax is applied. Therefore, the burden can be avoided in the case where the service provider is authorized to claim its right to deduction directly from the tax authorities once the tax has been levied. In such a case, the right to deduct is given as a reimbursement of a fraction of the tax withheld at source. In the end it is for the service provider to decide whether to invest resources in demonstrating the genuineness and the actual amount of business expenses which it seeks to deduct.
concluded tax treaties with Iceland, Liechtenstein and Norway. Consequently, the ECJ held that the legislation at issue, in relation to third countries that are parties to the EEA Agreement does not go beyond what is necessary to attain the effectiveness of fiscal supervision and prevention of tax avoidance.

Case C-503/14

European Commission v. Portuguese Republic

Decision date: 21 December 2016
Procedure type: Infringement procedure
AG opinion: Wathelet, 12 May 2016
Justifications: Balanced allocation of taxing powers, coherence/cohesion of the tax system, fiscal supervision, prevention of abuse, territoriality
Decision type: Judgment
Legal basis: Art. 18 EC Treaty, Art. 21 TFEU (Right of EU citizens to move and reside freely within the EU)
Host State/Home State: Home State
Keywords: Individual income tax, exit tax, capital gains
Authentic language: Portuguese

Synopsis
Legislation of a Member State which immediately taxes the unrealized capital gains based solely on the transfer of tax residence outside of that Member State of an individual in comparison with the tax referral granted to an individual in a purely internal situation constitutes a restriction of the freedom of establishment and of the free movement of persons. In addition, tax rules which immediately tax the unrealized capital gains in case of transfer of assets and liabilities by an individual in return for shares in a company that has its head office and its effective management outside Portugal in comparison with the deferral of taxation of such gains in case of a purely internal situation constitute a restriction to the freedom of establishment.

Facts
The Commission referred Portugal to the ECJ due to its rules on taxation of (i) unrealized capital gains of taxable persons who transfer their residence outside Portugal and (ii) unrealized capital gains when the transfer of assets and liabilities by an individual is made in return for shares in a company that has its head office and its effective management outside Portugal.

Legal background and issue
According to the Portuguese tax law, taxable persons who continue to reside in Portugal benefit from a tax deferral on the capital gains resulting from the exchange of the shares until the subsequent disposal of the shares received upon
the exchange. Taxable persons who transfer their residence outside Portugal are obliged, as a result of that transfer, to immediately pay the capital gains tax resulting from that exchange.

Also, the Portuguese tax law provides that in the event of a transfer of assets and liabilities to a company that has its head office and its effective management in Portugal by an individual in exchange for shares, the taxation of capital gains only takes place when these assets and liabilities have been disposed of by the company which received them, provided that other conditions are also met. By contrast, when the transfer of assets and liabilities by an individual in exchange of shares is made to a company that has its head office and its effective management outside Portugal, the taxation of the unrealized capital gains is immediate.

The issues were:
(i) whether the tax rules providing for immediate taxation of the unrealized capital gains from the exchange of the shares of an individual based solely on the transfer of tax residence outside of that Member State constitutes a restriction of the freedom of establishment and also a restriction to the free movement of workers, as provided by the TFEU and the EEA Agreement and also Art. 21 of the TFEU; and
(ii) whether the tax rules providing for immediate taxation of the unrealized capital gains when transfer of assets and liabilities relating to an activity carried out on an individual basis is made in return for shares in a company that has its head office and its effective management outside Portugal constitutes a restriction of the freedom of establishment as provided by the TFEU and the EEA Agreement.

Decision

Scope
The case was decided in the light of the free movement of workers and freedom of establishment as provided by the TFEU and EEA Agreement as regards the first issue and based on the freedom of establishment as provided by the TFEU and EEA Agreement as regards the second issue.

Discrimination/restriction
As regards the first issue, taxable persons who continue to reside in Portugal benefit from a tax deferral on the capital gains resulting from the exchange of the shares until the subsequent disposal of the shares received upon the exchange. Taxable persons who transfer their residence outside Portugal are obliged, as a result of that transfer, to pay the capital gains tax resulting from that exchange immediately. That difference in treatment as regards the time of taxation of the capital gains at issue constitutes a cash flow disadvantage for the taxable person who wishes to transfer his residence outside Portugal. The exclusion of a cash flow advantage in a cross-border situation where it is available in an equivalent domestic situation represents a restriction on the free movement of workers and the freedom of establishment as provided by the TFEU and EEA Agreement, considering that the individuals are in a comparable situation from the point of view of the legislation of that Member State aiming to tax capital gains generated in its territory.
As regards the second issue, individuals transferring all the assets to a company with its head office and effective management in Portugal, the capital gains tax must be paid by the transferee company at the time of the subsequent disposal of the assets, whereas individuals transferring all of those assets to a company with its head office or effective management out of Portugal become liable to capital gains tax at the time of such a transfer. This difference in treatment results in a cash flow disadvantage for an individual who transfers all the assets to a company with its head office or effective management outside Portugal, and thus constitutes a restriction to the freedom of establishment as provided by the TFEU and the EEA Agreement.

Justifications

Justifications for the first issue
(i) *Balanced allocation of the taxing rights*. This justification was rejected by the ECJ as the provisions of national law do not leave the choice to the taxable person who transfers his residence from Portugal to another Member State to opt between the immediate payment of the tax on capital gains resulting from an exchange of shares and the deferred payment of the tax, which necessarily involves an administrative burden for the taxable person, in connection with tracing the transferred assets and accompanied by a bank guarantee.

(ii) *The need to preserve the cohesion of the tax system*. This justification was also rejected by the ECJ as Portugal has not shown that there is a direct link between the tax advantage provided for in the national provision at issue and the offsetting of that advantage by a particular tax levy.

The need to ensure the effectiveness of fiscal supervision and the prevention of tax avoidance and evasion were not accepted by the ECJ as possible justifications due to the fact that they were just mentioned by Portugal without being developed.

Justifications for the second issue
(i) *Balanced allocation of the taxing rights*. This justification was rejected due to the same reasons as in the case of the first issue.

(ii) *The need to guarantee economic continuity*. This justification was rejected by the ECJ as such an objective may be ensured without the need to distinguish between a purely internal situation and a cross-border situation.
1.2.9. Tax treaties

Case C-336/96
Gilly v. Directeur des services fiscaux du Bas-Rhin

Synopsis
In the absence of unifying or harmonizing measures for the elimination of double taxation on Community level, the Member States are competent to determine the criteria for allocating the powers of taxation between themselves, with a view to eliminate double taxation, by means of, inter alia, tax treaties. Art. 293 of the EC Treaty providing for negotiations between Member States to avoid double taxation does not have direct effect. The freedom of employment does not oblige Member States to refund excess foreign tax credits on employment income.

Facts
Mr. and Mrs. Gilly were teachers who resided in France. Mr. Gilly, a French national, taught in France, whereas Mrs. Gilly, a German national who also acquired French nationality by marriage, taught in a state school in the frontier area of Germany. Pursuant to the Germany–France tax treaty, the public-service remuneration received by Mrs. Gilly in Germany from 1989 until 1993 was taxed in Germany. It was also taxed in France, but France granted an ordinary tax credit for the tax paid in Germany. In the case of Mrs. Gilly, such tax credit was less than the tax actually paid in Germany on the German-source income. Mr. and Mrs. Gilly brought proceedings against the tax authorities before the Adminis-
trative Court of Strasbourg, in which they claimed that the taxation of Mrs. Gilly’s German-source income according to the relevant tax treaty was contrary to EC law. The latter court referred questions for preliminary ruling to the ECJ.

**Legal background and issue**

The Germany–France tax treaty laid down a general rule regarding the taxation of employment income according to which such income was taxable where the personal activity in respect of which it was received was carried out. The tax treaty contained a special regime applicable to frontier workers. Such workers were normally taxed in their state of residence. However, if those frontier workers were working in the public sector, another special rule applied, i.e. their income was taxable in the state of the public body employing them as long as they held the nationality of that state, except when they also had the nationality of the other Contracting State, in which case they were taxable in their state of residence. The exception did not apply however when the civil servant had the nationality of both states, which was the case of Mrs. Gilly. Furthermore, the tax treaty also provided for a special rule for teachers who became temporary resident in the Contracting State where the school was where they were teaching, for a period of less than two years, were taxable in the other Contracting State of which originally they were a resident. The tax treaty provided for the credit method as a means of avoiding double taxation with respect to income from private or public employment.

Mrs. Gilly’s income, as she worked for a state school in Germany and she was a German national, fell under the special rule regarding public-service remuneration. Accordingly, her income was taxed in Germany, since she had both the French and German nationality. Because she was also taxed in France, however, she received a tax credit that could have been set off against the French tax that was due on her household’s total income taxable in France. According to the relevant tax treaty provision that tax credit could not exceed the fraction of French tax corresponding to the German-source income (ordinary tax credit). In the case of Mrs. Gilly the tax credit proved to be less than the actual tax paid in Germany because of the greater progressivity of the tax scale in Germany. Moreover, personal and family circumstances were not taken into account in the state of employment, Germany, whereas they were taken into account in the state of residence, France, when calculating the tax on the total income, which also resulted in the tax credit being lower than the amount of German tax actually paid.

The referring national court had doubts about the compatibility of the above provisions of the Germany–France tax treaty with Art. 39 of the EC Treaty. In particular, the court wondered whether the use of various connecting factors, such as nationality and residence, by the tax treaty as a basis for establishing differing tax regimes with regard to the taxation of employment income is in accordance with the freedom of movement of workers. In addition, the national court sought guidance on the tax credit mechanism under the tax treaty, which was claimed to be penalizing those who had exercised their freedom of movement by allowing a degree of double taxation to remain. Finally the national court raised the issue whether Art. 293 providing for the elimination of double taxation by tax treaties had direct effect.
The national court, in essence, asked whether or not the freedom of movement for workers precludes the application of the provisions of the Germany-France tax treaty, under which

(i) the tax regime applicable to frontier workers differs depending on whether they work in the private or public sector;
(ii) in case of frontier workers working in the public sector, the regime differs depending on the nationality of which Contracting State they possess;
(iii) the regime applicable to teachers differs depending on whether their residence in the state in which they are teaching is for a short period or not;
(iv) a tax credit mechanism is provided for that allows frontier workers who are taxed both in their state of employment and their state of residence to be taxed more heavily than persons who receive employment income only in their state of residence; and
(v) finally, whether a taxpayer derives an individual right from Art. 293, providing for the abolition of double taxation through bilateral negotiations.

**Decision**

**Scope**
The case falls within the scope of the freedom of movement for workers. The ECJ rejected the French government’s argument that Mrs. Gilly, who worked in her state of origin (Germany) has not exercised in France the freedom conferred on her by Art. 39 of the EC Treaty. The ECJ pointed out that the case concerns a German national, who acquired the French nationality by marriage, working in Germany whilst residing in France. Thus, she must be considered in France as a worker exercising her right to freedom of movement in order to work in a Member State other than her state of residence.

**Discrimination/restriction**
The ECJ held that the challenged provisions in the Germany–France tax treaty were not precluded by the freedom of movement for workers. Although abolition of double taxation within the Community is one of the objectives of the EC Treaty, it was pointed out that, apart from the Arbitration Convention, no unifying or harmonizing measure for the elimination of double taxation has yet been adopted at Community level, nor have the Member States yet concluded any multilateral convention to that effect under Art. 293 of the EC Treaty. The Member States are competent to determine the criteria for taxation on income and wealth with a view to eliminate double taxation by means of, inter alia, international agreements.

The fact that the Germany–France tax treaty lays down different connecting factors depending on whether the taxpayer is a frontier worker or not, is a teacher in short-term residence or not, or is employed in the private or public sector has to be considered against this background. Although the criterion of nationality appears among the connecting factors for the purpose of allocating tax jurisdiction, such differentiation cannot be regarded as constituting discrimination precluded by Art. 39 of the EC Treaty. This flows, in the absence of any unifying or harmonizing measures under EC law, from the contracting parties’ competence to define the criteria for allocating their powers of taxation between themselves, with a view to eliminate double taxation.
Furthermore, the allocation of the taxing rights under the Germany–France tax treaty regarding public-service remuneration follows Art. 19 of the OECD Model Convention, which reflects international practice. In addition, disadvantageous taxation cannot follow from the choice of a connecting factor in itself. Whether the tax treatment of the taxpayers concerned is favourable or unfavourable is determined not, strictly speaking, by the choice of the connecting factor, but by the level of taxation in the competent state, in the absence of any EC harmonization of scales of direct taxation.

As regards the issue of the ordinary tax credit, the ECJ first observed that the objective of a tax treaty is not to ensure that the taxpayer is not subjected to higher tax in one state than he would be in another, but to prevent the same income from being taxed in each of the two states. The unfavourable consequences of the tax credit mechanism are the result of the differences between the tax scales of the Member States and in the absence of any Community legislation in the field, the determination of those scales is a matter for the Member States. Furthermore, the fact that the taxpayer’s personal and family circumstances were taken into account in the state of residence but not in the state of employment were in line with the Schumacker-principle. Germany, as the state of employment, was not obliged to have regard to such circumstances of Mrs. Gilly, since they were taken into account in France, the state of residence, which is, in general, in the best position to assess those circumstances.

In giving its answer to the national court, the ECJ also clarified that Art. 293 of the EC Treaty, which defines the abolition of double taxation within the Community as an objective for the Member States, does not have direct effect. It is clear from the wording of that provision that it cannot itself confer on individuals any rights on which they might be able to rely before their national courts.
The national court, in essence, asked whether or not the freedom of movement for workers precludes the application of the provisions of the Germany-France tax treaty, under which

(i) the tax regime applicable to frontier workers differs depending on whether they work in the private or public sector;
(ii) in case of frontier workers working in the public sector, the regime differs depending on the nationality of which Contracting State they possess;
(iii) the regime applicable to teachers differs depending on whether their residence in the state in which they are teaching is for a short period or not;
(iv) a tax credit mechanism is provided for that allows frontier workers who are taxed both in their state of employment and their state of residence to be taxed more heavily than persons who receive employment income only in their state of residence; and
(v) finally, whether a taxpayer derives an individual right from Art. 293, providing for the abolition of double taxation through bilateral negotiations.

**Decision**

**Scope**
The case falls within the scope of the freedom of movement for workers. The ECJ rejected the French government’s argument that Mrs. Gilly, who worked in her state of origin (Germany) has not exercised in France the freedom conferred on her by Art. 39 of the EC Treaty. The ECJ pointed out that the case concerns a German national, who acquired the French nationality by her marriage, working in Germany whilst residing in France. Thus, she must be considered in France as a worker exercising her right to freedom of movement in order to work in a Member State other than her state of residence.

**Discrimination/restriction**
The ECJ held that the challenged provisions in the Germany–France tax treaty were not precluded by the freedom of movement for workers. Although abolition of double taxation within the Community is one of the objectives of the EC Treaty, it was pointed out that, apart from the Arbitration Convention, no unifying or harmonizing measure for the elimination of double taxation has yet been adopted at Community level, nor have the Member States yet concluded any multilateral convention to that effect under Art. 293 of the EC Treaty. The Member States are competent to determine the criteria for taxation on income and wealth with a view to eliminate double taxation by means of, inter alia, international agreements.

The fact that the Germany–France tax treaty lays down different connecting factors depending on whether the taxpayer is a frontier worker or not, is a teacher in short-term residence or not, or is employed in the private or public sector has to be considered against this background. Although the criterion of nationality appears among the connecting factors for the purpose of allocating tax jurisdiction, such differentiation cannot be regarded as constituting discrimination precluded by Art. 39 of the EC Treaty. This flows, in the absence of any unifying or harmonizing measures under EC law, from the contracting parties’ competence to define the criteria for allocating their powers of taxation between themselves, with a view to eliminate double taxation.