Case C-182/06

État du Grand-Duché de Luxembourg

v

Hans Ulrich Lakebrink and Katrin Peters-Lakebrink

(Reference for a preliminary ruling from the Cour administrative)

(Article 39 EC – Income tax payable by non?residents – Calculation of tax rate – Properties in another Member State – Negative rental income not taken into account)

Opinion of Advocate General Mengozzi delivered on 29 March 2007

Judgment of the Court (First Chamber), 18 July 2007

Summary of the Judgment

Freedom of movement for persons – Workers – Equal treatment – Remuneration – Income tax

(Art. 39 EC)

Article 39 EC is to be interpreted as precluding national legislation which does not entitle a Community national who is not resident in the Member State in which he receives income that constitutes the major part of his taxable income to request, for the purposes of determination of the tax rate applicable to the income so received, that negative rental income relating to property situated in another Member State which he does not himself occupy be taken into account, whilst a resident of the first State can request that such negative rental income be taken into account.

In relation to direct taxes, the situations of residents and non?residents are, as a rule, not comparable. Consequently, the fact that a Member State does not grant to a non?resident taxpayer certain tax advantages which it grants to resident taxpayers is not, as a rule, discriminatory, since those two categories of taxpayer are not in a comparable situation.

The position is different, however, where the non-resident receives no significant income in his State of residence and obtains the major part of his taxable income from an activity performed in the State of employment, with the result that the State of his residence is not in a position to grant him the advantages resulting from the taking into account of his personal and family circumstances. Discrimination arises from the fact that those circumstances are taken into account neither in the State of residence nor in the State of employment.

The ground on which that finding of discrimination is based concerns all the tax advantages connected with the non?resident’s ability to pay tax which are not taken into account either in the State of residence or in the State of employment, since the ability to pay tax forms part of the personal situation of the non?resident.

(see paras 28-31, 34, 36, operative part)

JUDGMENT OF THE COURT (First Chamber)

18 July 2007 (*)

(Article 39 EC – Income tax payable by non?residents – Calculation of tax rate – Properties in another Member State – Negative rental income not taken into account)

In Case C?182/06,

REFERENCE for a preliminary ruling under Article 234 EC from the Cour administrative (Luxembourg), made by decision of 6 April 2006, received at the Court on 10 April 2006, in the proceedings

État du Grand-Duché de Luxembourg

v

Hans Ulrich Lakebrink,

Katrin Peters?Lakebrink,

THE COURT (First Chamber),

composed of P. Jann, President of the Chamber, R. Schintgen, A. Tizzano, M. Ileši? and E. Levits (Rapporteur), Judges,

Advocate General: P. Mengozzi,

Registrar: R. Grass,

having regard to the written procedure,

after considering the observations submitted on behalf of:

– État du Grand?Duché de Luxembourg, by C. Schiltz, acting as Agent,

– Mr Lakebrink and Mrs Peters?Lakebrink, by M. Kleyr, avocat,

– the Netherlands Government, by H.G. Sevenster and M. de Mol, acting as Agents,

– the Swedish Government, by K. Wistrand, acting as Agent,

– the Commission of the European Communities, by R. Lyal and J.?P. Keppenne, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 29 March 2007,

gives the following

Judgment

1 This reference for a preliminary ruling concerns Article 39 EC.

2 The reference was made in the course of proceedings between the State of the Grand Duchy of Luxembourg (État du Grand?Duché de Luxembourg) and Mr Lakebrink and Mrs Peters?Lakebrink (‘Mr and Mrs Lakebrink’) concerning their income tax liability in Luxembourg for the year 2002.

Legal context, the dispute in the main proceedings and the question referred for a preliminary ruling

3 Mr and Mrs Lakebrink, German nationals resident in Germany, were both employed exclusively in Luxembourg. For the year 2002, they applied in Luxembourg for joint tax assessment within the meaning of Article 157ter of the Law of 4 December 1967 on income tax, as amended (‘the LIR’).

4 In their tax return to the Luxembourg tax authorities, Mr and Mrs Lakebrink declared negative rental income of EUR 26 080 in connection with two properties in Germany which they own but do not occupy themselves. They applied for this rental loss to be taken into account for the purposes of determining the tax rate applicable to residents.

5 On 30 July 2003, the Finanzamt Trier (Tax Office, Trier, Germany) issued to Mr and Mrs Lakebrink an income tax notice for the year 2002 in which the negative rental income was duly noted. It is clear from that income tax notice that Mr and Mrs Lakebrink did not receive taxable income in Germany. Consequently, they did not pay tax there.

6 As requested, Mr and Mrs Lakebrink were taxed jointly in Luxembourg. Pursuant to Article 157ter of the LIR, tax was calculated at the rate which would have applied if they had been Luxembourg residents. The negative rental income from their properties in Germany was not, however, taken into consideration for the purposes of determining the rate.

7 Article 157ter of the LIR provides that – in derogation from the tax regime applicable to resident taxpayers according to which the progressivity rule is to apply, when calculating the tax rate, to all income which other States are entitled to tax – under the tax regime applicable to non?resident taxpayers and in accordance with Article 134 of the LIR, the progressivity clause is to apply, apart from to local income, only to the foreign earned income of non?resident taxpayers.

8 In accordance with Article 4 of the Convention concluded on 23 August 1958 between the Grand Duchy of Luxembourg and the Federal Republic of Germany for the avoidance of double taxation and the establishment of rules relating to mutual administrative assistance in the fields of income tax, wealth tax, local business tax and property tax, the right to tax income from the letting of immoveable property falls to the State in which the property is situated, which is, in the present case, the Federal Republic of Germany.

9 Mr and Mrs Lakebrink lodged an objection against the income tax notice issued by the Luxembourg tax authorities, which never received a reply. They brought an action seeking rectification of that notice before the Luxembourg Tribunal administratif (Administrative Court), which declared their action well founded.

10 The State of the Grand Duchy of Luxembourg appealed against that decision to the Cour administrative (Higher Administrative Court). That court is uncertain inter alia whether the application of Article 157ter of the LIR, inasmuch as it entails the refusal to take the negative rental income from Mr and Mrs Lakebrink's properties in Germany into consideration for the purpose of determining the tax rate applicable to their Luxembourg income, constitutes indirect discrimination which is prohibited by Article 39 EC.

11 In those circumstances, the Cour administrative decided to stay the proceedings and to refer the following question to the Court for a preliminary ruling:

'Is Article 39 EC to be interpreted as precluding national rules, such as those introduced in ... Luxembourg by Article 157ter of the [LIR], under which a Community national not resident in Luxembourg who receives income of Luxembourg origin from employment, which constitutes the major part of his taxable income, cannot rely on his negative rental income relating to property situated in another Member State, in this case Germany, which he does not himself occupy, for the purposes of the determination of the tax rate applicable to his Luxembourg income?'

The question referred for a preliminary ruling

12 By its question, the national court asks, essentially, whether Article 39 EC is to be interpreted as precluding national legislation such as that at issue in the main proceedings under which a Community national who is not resident in the Member State in which he receives income that constitutes the major part of his taxable income cannot, for the purposes of determination of the tax rate applicable to the income so received, rely on negative rental income relating to property situated in another Member State which he does not himself occupy, whilst a resident of the first State can rely on such negative rental income.

13 The legislation at issue in the main proceedings lays down a different tax regime depending on whether or not a worker receiving the major part of his taxable income in Luxembourg is resident there.

14 It must be stated, first, that although direct taxation does not as such fall within the purview of the European Community, the powers retained by the Member States must nevertheless be exercised consistently with Community law (see, inter alia, Case C?279/93 *Schumacker* [1995] ECR I?225, paragraph 21, and Case C?290/04 *FKP Scorpio Konzertproduktionen* [2006] ECR I?9461, paragraph 30).

15 It should also be noted that any Community national who, irrespective of his place of residence and his nationality, works in a Member State other than that of residence falls within the scope of Article 39 EC (see Case C?152/03 *Ritter-Coulais* [2006] ECR I-1711, paragraph 31).

16 It follows that the situation of Mr and Mrs Lakebrink, who were working in a Member State other than that in which they had their residence, falls within the scope of Article 39 EC.

17 Finally, it is settled case?law that all of the provisions of the EC Treaty relating to freedom of movement for persons have the purpose of facilitating the pursuit by Community nationals of occupational activities of all kinds throughout the Community and preclude measures which might

place Community nationals at a disadvantage when they wish to pursue an economic activity in the territory of another Member State (Case C?302/98 *Sehrer* [2000] ECR I?4585, paragraph 32, and Case C?209/01 *Schilling and Fleck-Schilling* [2003] ECR I?13389, paragraph 24).

18 Unlike persons working and residing in Luxembourg, Mr and Mrs Lakebrink, who were working in Luxembourg but resident in Germany, were not entitled according to Luxembourg legislation to request that the rental income losses from their properties in Germany be taken into account for the purpose of determining the tax rate for their Luxembourg income.

19 Accordingly, the treatment reserved by the legislation at issue in the main proceedings for non?resident workers, such as Mr and Mrs Lakebrink, is less favourable than that to which resident workers are entitled.

20 The Luxembourg and Netherlands Governments submit, on the contrary, that, inasmuch as that legislation takes no account of unearned foreign income, whether negative or positive, it affords non?resident taxpayers a tax regime which is, overall, favourable compared to that of resident taxpayers.

21 Such a global assessment of the effects of the legislation cannot be upheld, because it would effectively render the prohibition laid down by Article 39 EC meaningless.

22 Although legislation such as that at issue in the main proceedings may offer a tax advantage to non?resident taxpayers declaring unearned foreign income where that income is positive or at least mostly positive, the case is different for non?resident taxpayers such as Mr and Mrs Lakebrink, who have only negative unearned foreign income.

23 As the Advocate General observes at point 29 of his Opinion, the fact that, in a situation such as that in the main proceedings, the legislation at issue places non?residents at a disadvantage cannot be compensated for by the fact that in other situations that same legislation does not discriminate between non?residents and residents.

24 It is settled case?law that unfavourable tax treatment contrary to a fundamental freedom cannot be justified by the existence of other tax advantages, even supposing that such advantages exist (see Case C?385/00 *de Groot* [2002] ECR I?11819, paragraph 97 and the case?law cited).

25 Moreover, in the absence of taxable income in their State of residence, workers such as Mr and Mrs Lakebrink are unable to request that rental income losses from their properties in that State to be taken into account and are therefore denied any possibility of relying on their negative rental income for the purpose of determining the tax rate for the whole of their income.

26 In those circumstances, it is necessary to determine whether the tax disadvantage which affects workers who are not resident in Luxembourg, such as Mr and Mrs Lakebrink, is capable of amounting to indirect discrimination on the basis of nationality prohibited by Article 39 EC.

27 It is settled case?law that discrimination can arise only through the application of different rules to comparable situations or the application of the same rule to different situations (*Schumacker*, paragraph 30; Case C?311/97 *Royal Bank of Scotland* [1999] ECR I-2651, paragraph 26; and Case C?383/05 *Talotta* [2007] ECR I-0000, paragraph 18).

28 In relation to direct taxes, the situations of residents and non?residents are, as a rule, not comparable (*Schumacker*, paragraph 31).

29 Consequently, the fact that a Member State does not grant to a non?resident taxpayer certain tax advantages which it grants to resident taxpayers is not, as a rule, discriminatory, since

those two categories of taxpayer are not in a comparable situation.

30 According to well?established case law, the position is different, however, where the non-resident receives no significant income in his State of residence and obtains the major part of his taxable income from an activity performed in the State of employment, with the result that the State of his residence is not in a position to grant him the advantages resulting from the taking into account of his personal and family circumstances (see, in particular, *Schumacker*, paragraph 36).

31 According to the same case?law, discrimination arises from the fact that the personal and family circumstances of a non?resident who receives the major part of his income and almost all his family income in a Member State other than that of his residence are taken into account neither in the State of residence nor in the State of employment (*Schumacker*, paragraph 38).

32 That case?law applies to a situation such as that in the main proceedings.

33 First, the discrimination referred to at paragraph 31 of the present judgment a fortiori concerns non?resident workers, such as Mr and Mrs Lakebrink, who, as stated at paragraph 25 of the present judgment, receive no income in their State of residence and obtain all their family income from an activity performed in the State of employment.

34 Secondly, the ground, recalled at paragraph 31 of the present judgment, on the basis of which the Court made its finding of discrimination in *Schumacker* concerns, as the Advocate General has pointed out at point 36 of his Opinion, all the tax advantages connected with the non?resident's ability to pay tax which are not taken into account either in the State of residence or in the State of employment (see also the Opinion of Advocate General Léger in *Ritter-Coulais*, points 97 to 99), since the ability to pay tax may indeed be regarded as forming part of the personal situation of the non?resident within the meaning of the judgment in *Schumacker*.

35 Consequently, the refusal by a Member State's tax authorities to take into consideration negative rental income concerning a taxpayer's properties abroad constitutes discrimination prohibited by Article 39 EC.

36 Having regard to the foregoing, the answer to the question referred must be that Article 39 EC is to be interpreted as precluding national legislation which does not entitle a Community national who is not resident in the Member State in which he receives income that constitutes the major part of his taxable income to request, for the purposes of determination of the tax rate applicable to the income so received, that negative rental income relating to property situated in another Member State which he does not himself occupy be taken into account, whilst a resident of the first State can request that such negative rental income be taken into account.

Costs

37 Since these proceedings are, for the parties to the main proceedings, a step in the action pending before the national court, the decision on costs is a matter for that court. Costs incurred in submitting observations to the Court, other than the costs of those parties, are not recoverable.

On those grounds, the Court (First Chamber) hereby rules:

Article 39 EC is to be interpreted as precluding national legislation which does not entitle a Community national who is not resident in the Member State in which he receives income that constitutes the major part of his taxable income to request, for the purposes of determination of the tax rate applicable to the income so received, that negative rental income relating to property situated in another Member State which he does not himself occupy be taken into account, whilst a resident of the first State can request that such negative rental income be taken into account.

[Signatures]

*Language of the case: French.