

JUDGMENT OF THE COURT (Second Chamber)

30 June 2016 (*)

(Reference for a preliminary ruling — Taxation — Free movement of capital — Inheritance tax — Legislation of a Member State providing for a reduction in inheritance tax applicable to estates containing assets which have already formed part of an inheritance giving rise to the imposition of inheritance tax in that Member State — Restriction — Justification — Coherence of the tax system)

In Case C-123/15,

REQUEST for a preliminary ruling under Article 267 TFEU from the Bundesfinanzhof (Federal Finance Court, Germany), made by decision of 20 January 2015, received at the Court on 12 March 2015, in the proceedings

Max-Heinz Feilen

v

Finanzamt Fulda,

THE COURT (Second Chamber),

composed of M. Ilešič, President of the Chamber, C. Toader, A. Rosas, A. Prechal and E. Jarašiūnas (Rapporteur), Judges,

Advocate General: M. Wathelet,

Registrar: I. Illéssy, Administrator,

having regard to the written procedure and further to the hearing on 27 January 2016,

after considering the observations submitted on behalf of:

- Mr Feilen, by P. Thouet, Rechtsanwalt,
- the German Government, by T. Henze, acting as Agent,
- the Spanish Government, by A. Rubio González, acting as Agent,
- the United Kingdom Government, by S. Sutton and M. Holt, acting as Agents, and by R. Hill, Barrister,
- the European Commission, by M. Wasmeier and W. Roels, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 17 March 2016,

gives the following

Judgment

1 This request for a preliminary ruling concerns the interpretation of Articles 63(1) TFEU and 65 TFEU.

2 The request has been made in proceedings between Mr Max-Heinz Feilen and the Finanzamt Fulda (Fulda Tax Office, Germany) concerning the latter's refusal to grant Mr Feilen the benefit of a reduction in the inheritance tax to which his mother's estate is subject.

Legal context

3 Paragraph 1(1)(1) of the Erbschaftsteuer- und Schenkungsteuergesetz (the German Law on Inheritance and Gift Tax; 'the ErbStG'), in the version applicable to the 2007 tax year, makes acquisitions received by reason of death subject to inheritance tax.

4 Under Paragraph 2(1)(1) to (3) of the ErbStG:

'Liability to tax arises:

1. In the cases referred to in Paragraph 1(1)(1) to (3), in relation to the entire estate if the deceased, at the date of death, ... or the recipient, at the date of the taxable event, is a resident. The following are deemed to be residents:

(a) natural persons whose permanent residence or habitual residence is in Germany,

...

3. In all other cases, in relation to transferred assets which are domestic assets within the meaning of Paragraph 121 of the Bewertungsgesetz [Law on Valuation] ...'

5 Paragraph 15 of the ErbStG, which defines tax classes, provides, in subparagraph 1:

'According to the personal relationship between the beneficiary and the deceased or donor, the following three tax classes are distinguished:

Tax Class I:

1. the spouse or civil partner;
2. the children and step-children;
3. descendants of the children and step-children in No 2;
4. relatives in the ascending line in cases of inheritance:

...'

6 With regard to reductions in inheritance tax, Paragraph 27 of the ErbStG contains the following provisions:

'(1) Where a person in Tax Class I inherits an asset which, in the 10 years preceding that acquisition, has already been transferred to a person in that tax class and has given rise to the imposition of inheritance tax under this law, the amount of tax payable is, subject to the provisions of subparagraph 3, reduced as follows:

by ...%

where the period between the two dates on which the liability to tax arose is

50

less than 1 year

45

between 1 year and 2 years

40

between 2 years and 3 years

35

between 3 years and 4 years

30

between 4 years and 5 years

25

between 5 years and 6 years

20

between 6 years and 8 years

10

between 8 years and 10 years

...

(3) The reduction referred to in subparagraph 1 may not exceed the amount which results from the application of the percentage rates specified in subparagraph 1 to the inheritance tax which the previous transferee paid in respect of the acquisition of the same asset.'

The dispute in the main proceedings and the question referred for a preliminary ruling

7 Mr Feilen, who is resident in Germany, is the sole heir of his mother, who died in 2007 in Germany, where she was last resident. His mother's estate consisted mainly of her share in the estate of her deceased daughter who died in 2004 in Austria, where the mother had also lived until her daughter's death. The distribution of the daughter's estate took place in Austria only after the mother's death, with the result that the inheritance tax on that estate, amounting to EUR 11 961.91, was paid by Mr Feilen.

8 In the tax return relating to his mother's estate, Mr Feilen claimed the inheritance tax paid by him in Austria as a liability of the estate and applied for a reduction, pursuant to Paragraph 27 of the ErbStG, in the amount of inheritance tax due. In its assessment of 28 October 2009, the Fulda Tax Office deducted the inheritance tax paid in Austria as a liability of the estate, but refused to

allow any reduction in the inheritance tax.

9 The Finanzgericht (Finance Court, Germany) dismissed the action lodged by Mr Feilen against that assessment on the grounds that Paragraph 27(1) of the ErbStG presupposed a previous inheritance that had been taxed under that law. However, that was not the situation in the present case, as the previous acquisition by the mother of her daughter's estate had not been subject to inheritance tax in Germany because neither the mother nor the daughter was, at the time of the latter's death, resident in Germany within the meaning of Paragraph 2(1)(1) of the ErbStG, and as the estate did not include domestic assets within the meaning of Paragraph 2(1)(3) of the ErbStG.

10 The Bundesfinanzhof (Federal Finance Court, Germany), before which an appeal on a point of law ('Revision') has been brought, expresses doubts as to whether Paragraph 27 of the ErbStG is compatible with EU law.

11 The Bundesfinanzhof notes, first, that the inheritance which the applicant in the main proceedings received may come within the scope of the EU-law provisions on the movement of capital. According to the Bundesfinanzhof, the inheritance received by Mr Feilen from his mother should not be regarded as a purely domestic transaction because the mother's assets consist essentially of her share in her daughter's estate in Austria.

12 Second, the referring court states that the refusal to allow a reduction in inheritance tax pursuant to Paragraph 27(1) of the ErbStG might, in the light of the Court's case-law, constitute a restriction on the movement of capital, since its effect is to reduce the value of an estate which includes an asset which has been subject to foreign inheritance tax. In that regard, the referring court expresses its doubts as to whether, in light of the Court's judgment of 12 February 2009 in *Block* (C?67/08, EU:C:2009:92), the existence of such a restriction is to be excluded.

13 Third, the referring court is unsure whether a possible restriction on the free movement of capital resulting from Paragraph 27(1) of the ErbStG is justified under the provisions of the TFEU.

14 It was in those circumstances that the Bundesfinanzhof (Federal Finance Court) decided to stay the proceedings and to refer the following question to the Court:

'Does the free movement of capital guaranteed by Article 63(1) TFEU in conjunction with Article 65 TFEU preclude legislation of a Member State which provides for a reduction in inheritance tax in the case of an inheritance by persons in a particular tax class where the estate includes assets that were already acquired by persons in that tax class during the ten years preceding the acquisition and inheritance tax was assessed in the Member State in respect of this previous acquisition, whereas a tax reduction is excluded where inheritance tax was levied in another Member State in respect of the previous acquisition?'

Consideration of the question referred

15 By its question the referring court asks, in essence, whether Articles 63(1) TFEU and 65 TFEU preclude legislation of a Member State, such as that at issue in the main proceedings, which provides for a reduction in inheritance tax in the case of an inheritance by persons in a particular tax class where the estate includes assets that were already acquired by persons in that tax class during the ten years prior to the acquisition, on the condition that inheritance tax was levied in another Member State in respect of the earlier acquisition.

16 As the referring court has observed, inheritances consisting in the transfer to one or more persons of assets left by a deceased person constitute, according to the settled case-law of the

Court, movements of capital within the meaning of Article 63 TFEU, except in cases where their constituent elements are confined within a single Member State (see, to that effect, judgments of 23 February 2006 in *van Hilten-van der Heijden*, C?513/03, EU:C:2006:131, paragraphs 39 to 42; of 17 January 2008 in *Jäger*, C?256/06, EU:C:2008:20, paragraphs 24 and 25; of 17 October 2013 in *Welte*, C?181/12, EU:C:2013:662, paragraphs 19 and 20; and of 3 September 2014 in *Commission v Spain*, C?127/12, not published, EU:C:2014:2130, paragraphs 52 and 53).

17 The estate at issue in the main proceedings in the present case contains an asset deriving from a previous inheritance involving Mr Feilen's sister and his mother in Austria where that asset was then located and where his sister and mother were resident at the time of the sister's death. That cross-border element is the reason why the inheritance tax reduction provided for under Paragraph 27 of the ErbStG was not granted to Mr Feilen. Since such a situation cannot be regarded as a purely domestic situation, the inheritance at issue in the main proceedings constitutes a transaction that qualifies as a movement of capital within the meaning of Article 63(1) TFEU.

18 It is therefore necessary to examine whether national legislation such as that at issue in the main proceedings constitutes a restriction on the movement of capital within the meaning of Article 63(1) TFEU and, if it does, whether such a restriction is justified.

Whether there is a restriction on the movement of capital

19 The Court has already ruled that legislation of a Member State which makes the application of an inheritance tax advantage, such as a tax-free allowance, dependent on the place of residence of the deceased person or the heir, or on the location of the assets contained in the estate, constitutes a restriction on the free movement of capital prohibited by Article 63(1) TFEU when it has the result that inheritances involving non-residents or containing assets located in another Member State are subject to a higher tax liability than that imposed on inheritances involving only residents or containing only assets located in the Member State of taxation, and which, therefore, has the effect of reducing the value of the inheritance (see, to that effect, judgments of 17 January 2008 in *Jäger*, C?256/06, EU:C:2008:20, paragraphs 30 to 35; of 17 October 2013 in *Welte*, C?181/12, EU:C:2013:662, paragraphs 23 to 26; of 3 September 2014 in *Commission v Spain*, C?127/12, not published, EU:C:2014:2130, paragraphs 57 to 60; and of 4 September 2014 in *Commission v Germany*, C?211/13, not published, EU:C:2014:2148, paragraphs 40 to 43).

20 In the present case, Paragraph 27(1) of the ErbStG provides that a reduction in inheritance tax is to be granted for the acquisition, by way of inheritance, of an asset by persons who come within Tax Class I if that asset, during the ten years prior to the acquisition, has already been acquired by persons coming within that tax class and that previous inheritance has given rise to the imposition of inheritance tax in Germany. Since such taxes are levied, under Paragraph 2 of the ErbStG, when the deceased person, at the date of death, or the recipient, at the date of the taxable event, are domiciled or resident within the national territory or when the assets consist of 'domestic assets', the grant of the reduction in inheritance tax presupposes that the assets in question were located in Germany at the time of the previous inheritance or, if they were located abroad, that at least one of the parties to that inheritance was resident in Germany.

21 That legislation therefore makes entitlement to the reduction in inheritance tax dependent on the location of the assets contained in the estate of the earlier inheritance and on the place of residence of the deceased or the beneficiary at the time of that earlier inheritance. The consequence of this is that an inheritance involving assets which were located in another Member State at the time of a previous inheritance in which none of the parties was resident in Germany is subject to higher inheritance tax than that levied in the case of an inheritance involving only assets

which were situated in Germany at the time of an earlier inheritance or involving assets which were situated in another Member State at the time of a previous inheritance at least one of the parties to which was resident in Germany. That legislation therefore has the effect, as noted by the referring court, of reducing the value of the inheritance.

22 It follows that national legislation such as that at issue in the main proceedings constitutes a restriction on the movement of capital within the meaning of Article 63(1) TFEU.

23 In view of the referring court's uncertainty as to whether the judgment of 12 February 2009 in *Block* (C-67/08, EU:C:2009:92) casts doubt on that conclusion, it should be noted that, unlike the situation examined in that judgment, the case in the main proceedings in the present case does not concern the double taxation of elements of the same inheritance by two Member States, but rather the tax treatment of an inheritance by one Member State which differs depending on whether or not it involves assets which have already given rise, in that Member State, to the imposition of tax at the time of an earlier inheritance.

Whether a restriction on the movement of capital can be justified

24 With regard to possible justification based on Article 65 TFEU, it must be recalled that, according to Article 65(1)(a) TFEU, Article 63 TFEU 'shall be without prejudice to the right of Member States ... to apply the relevant provisions of their tax law which distinguish between taxpayers who are not in the same situation with regard to their place of residence or with regard to the place where their capital is invested'.

25 In so far as that provision of Article 65 TFEU constitutes a derogation from the fundamental principle of the free movement of capital, it must be interpreted strictly. It cannot therefore be interpreted as meaning that all tax legislation which draws a distinction between taxpayers on the basis of their place of residence or of the Member State in which they invest their capital is automatically compatible with the Treaty. The derogation provided for in Article 65(1)(a) TFEU is itself limited by Article 65(3) TFEU, which provides that the national provisions referred to in paragraph 1 of that article 'shall not constitute a means of arbitrary discrimination or a disguised restriction on the free movement of capital and payments as defined in Article 63 [TFEU]' (judgment of 4 September 2014 in *Commission v Germany*, C-211/13, not published, EU:C:2014:2148, paragraph 46 and the case-law cited).

26 A distinction must therefore be made between the differences in treatment authorised under Article 65(1)(a) TFEU and the arbitrary discrimination prohibited under Article 65(3) TFEU. In that regard, the case-law of the Court makes it clear that, in order for national tax rules which, for the purposes of calculating inheritance or gift tax, distinguish between residents and non-residents, or between assets located within the national territory and those located outside that territory, to be able to be regarded as being compatible with the Treaty provisions on the free movement of capital, the difference in treatment must relate to situations which are not objectively comparable or must be justifiable by overriding reasons in the public interest (judgment of 3 September 2014 in *Commission v Spain*, C-127/12, not published, EU:C:2014:2130, paragraph 73 and the case-law cited).

27 As regards the comparability of the situations at issue, it is common ground that, for inheritance tax purposes, the legislation at issue in the main proceedings places on the same footing persons in Tax Class I and resident in the national territory who acquire by inheritance an estate involving assets that had already been acquired by persons in that tax class during the ten years preceding the acquisition, irrespective of where the assets are located or where the beneficiaries thereof were resident at the time of that previous inheritance. It is only for the application of the reduction in inheritance tax provided for under Paragraph 27(1) of the ErbStG

that that legislation treats those persons differently depending on whether the assets in question were or were not located within national territory at the time of the previous inheritance and as to whether the parties to that inheritance were or were not resident within that territory (see, by analogy, judgment of 17 October 2013 in *Welte*, C-181/12, EU:C:2013:662, paragraph 51 and the case-law cited).

28 It follows that the difference in treatment introduced by the legislation at issue in the main proceedings concerns situations which are objectively comparable.

29 It is thus necessary to examine whether such legislation can be objectively justified by an overriding reason in the general interest, such as the need to preserve the coherence of the tax system mentioned by the referring court and invoked by the German Government.

30 In that regard, it must be borne in mind that the Court has already recognised that the need to maintain the coherence of a tax system may justify a restriction on the exercise of the freedoms of movement guaranteed by the Treaty. However, in order for such justification to be accepted, a direct link must be established between the tax advantage concerned and the offsetting of that advantage by a particular tax levy, the direct nature of that link falling to be examined in the light of the objective pursued by the legislation in question (judgments of 17 October 2013 in *Welte*, C-181/12, EU:C:2013:662, paragraph 59, and of 7 November 2013 in *K*, C-322/11, EU:C:2013:716, paragraphs 65 and 66 and the case-law cited).

31 In the present case, the referring court has taken the view that the advantage resulting from the reduction in inheritance tax provided for under Paragraph 27(1) of the ErbStG is directly linked to the fact that there had already been an imposition of inheritance tax in respect of the previous acquisition by inheritance of the same asset. The referring court has specified that the objective of that provision is to reduce, in the case where there are multiple transfers of the same asset within a period of 10 years between persons in Tax Class I, by up to 50%, the inheritance tax relating to that asset in so far as it has resulted in the imposition of tax on the previous transferee.

32 That assessment is shared, in essence, by the German Government, which specifies that Paragraph 27 of the ErbStG is based on the idea that an asset is transferred between close relatives of one generation to the next generation and that a new tax on the same asset, when it has already been imposed in the recent past, is to some extent unfair. That paragraph is therefore intended to avoid in part double taxation of the same asset more than once within a short space of time by foregoing the imposition of a portion of the inheritance tax when such tax was levied in Germany on a previous inheritance within the periods set out in that paragraph. Not granting a reduction of those taxes in the case of an earlier acquisition exclusively taxed outside Germany is, it is submitted, objectively linked to the fact that the Federal Republic of Germany was unable to tax that acquisition and collect the corresponding tax revenues.

33 With regard to those considerations, it is apparent that, by providing that only persons receiving assets by way of an inheritance which has given rise to the imposition of such taxes in Germany can benefit from the reduction in inheritance tax, the configuration of that tax advantage reflects a logical symmetry (see judgments of 1 December 2011 in *Commission v Belgium*, C-250/08, EU:C:2011:793, paragraph 73, and in *Commission v Hungary*, C-235/09, EU:C:2011:795, paragraph 74). That logic would be disturbed if that tax advantage were also to benefit persons inheriting assets which did not give rise to the imposition of inheritance tax in that Member State.

34 It follows that, in that inheritance tax exemption scheme, there is a direct link between that tax advantage and the previous imposition.

35 Admittedly, the Court has held, in cases not coming within the field of inheritance tax, that there is no such direct link where a case relates, in particular, to different taxes or to the tax treatment of different taxpayers (see, to that effect, judgments of 18 September 2003 in *Bosal*, C?168/01, EU:C:2003:479, paragraph 30, and of 24 February 2015 in *Grünwald*, C?559/13, EU:C:2015:109, paragraph 49).

36 However, in a particular situation such as that contemplated in Paragraph 27 of the ErbStG, the condition that the same taxpayer must be involved could not be applied given that the person who paid the inheritance tax at the time of the earlier inheritance is necessarily deceased.

37 Furthermore, the objective pursued by Paragraph 27 of the ErbStG, as is clear from paragraphs 31 and 32 above, is to reduce to a certain extent the tax burden on an inheritance involving assets transferred between close relatives which had already given rise to a previous imposition, by preventing partially the double taxation in Germany of assets more than once within a short space of time. With regard to that objective, there is, as the Advocate General noted in point 71 of his Opinion, a direct link between the reduction in inheritance tax provided for by that paragraph and the previous imposition of inheritance tax, that tax advantage and that previous imposition relating to the same tax, the same asset, and the close relatives of the same family.

38 It must be held, consequently, that the need to safeguard the coherence of the tax system may justify the restriction on the movement of capital resulting from national legislation such as that at issue in the main proceedings.

39 Furthermore, in order for such a restriction to be justified, it must be appropriate and proportionate to the objective pursued (see, to that effect, judgments of 1 December 2011 in *Commission v Belgium*, C?250/08, EU:C:2011:793, paragraph 78, and in *Commission v Hungary*, C?253/098, EU:C:2011:795, paragraph 79).

40 In that regard, it must be held that a reduction in inheritance tax calculated by applying percentages by reference to the period which has elapsed between the two dates on which the liability to tax arose, and made subject to the condition that the asset has already given rise to the imposition of such taxes in Germany in the preceding ten years appears to be appropriate in order to attain the objective pursued in Paragraph 27 of the ErbStG, as described in paragraph 37 above. That reduction is, furthermore, proportionate with regard to that objective since the Federal Republic of Germany did not have the power to tax the previous inheritance. In those circumstances, limiting the benefit of that reduction to situations in which that asset gave rise to taxation in Germany appears proportionate in the light of that objective (see, to that effect, judgment of 1 December 2011 in *Commission v Hungary*, C?253/09, EU:C:2011:795, paragraphs 80 and 81).

41 It follows that the restriction on the movement of capital resulting from national legislation such as that at issue in the main proceedings is justified by the need to preserve the coherence of the tax system.

42 Consequently, the answer to the question referred is that Articles 63(1) TFEU and 65 TFEU do not preclude legislation of a Member State, such as that at issue in the main proceedings, which provides for a reduction in inheritance tax in the case of inheritance by persons within a particular tax class where the estate includes assets that had already been acquired, by way of inheritance, by persons within that tax class during the 10 years prior to the acquisition, on condition that inheritance tax was levied in that Member State in respect of that earlier acquisition.

Costs

43 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 (Second Chamber) hereby rules:

Articles 63(1) TFEU and 65 TFEU do not preclude legislation of a Member State, such as that at issue in the main proceedings, which provides for a reduction in inheritance tax in the case of inheritance by persons within a particular tax class where the estate includes assets that had already been acquired, by way of inheritance, by persons within that tax class during the 10 years prior to the acquisition, on condition that inheritance tax was levied in that Member State in respect of that earlier acquisition.

[Signatures]

* Language of the case: German.