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EU Most Favoured Nation treatment v. tax treaty shopping: re-evaluating the anti-abuse justification in the «rule of reason» doctrine*

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Abstract

Most Favoured Nation (from now on «MFN») treatment concept is closely connected with the non-discrimination principle since it implies that source country cannot subject an inbound investment to different treatment according to the origin of the investors, ultimately with regards their residence.

The paper traces (Chapter 2) the reasons according to which ECJ reject the principle of MFN treatment in the field of direct taxation when the benefit to be extended form an integral part of a DTC. Then, the ECJ's approach to MFN treatment is considered erroneous because of its «tautologic» reasoning, the muddle of the taxpayer's factual and legal situation with his «entitlement» to DTC's benefits and the confusion between «allocation» and «exercise» of taxing right when source state «unilaterally extend» its «domestic treatment» to a non-resident. The author argues that the Court implicitly recognizes the Member States' freedom of tax treaty «competition» that is capable of undermining the Internal Market neutrality.

A «substantial» EU principle of equality is theorized by the author as required by EU law to achieve the neutrality of the Internal Market. According to

this principle, non-residents in a similar «personal» factual and legal situation (only from the perspective of the source state) should receive equal treatment according to the «comparability test» (in the context of the «discrimination analysis»). From these premises, the author deduces the application of an EU MFN treatment principle to grant to non-residents in comparable situation same «tax treaty» benefits to avoid «horizontal discrimination» in breach of the fundamental freedoms in the field of direct taxation. The author considers the advantage of the implementation of the MFN treatment principle into the EU against treaty shopping.

Nevertheless, the author highlights that the simple application of such MFN treatment principle would let EU and non-EU investors benefit from an «abusive» double non-taxation and non-EU investors to do treaty shopping (by using EU resident «conduit» entities) to take advantage of the EU MFN treatment. The core of the paper discusses how the loopholes of the EU MFN treatment principle can be defused by the «antidote» of the anti-abuse justification in case of treaty shopping, taking inspiration from the recent ECJ «Danish cases». The «antidote» of the anti-abuse justification is considered capable to passing the «proportionality test» when MFN treatment would be benefit by a «conduit» company or results in an «additional» benefit.

The paper considers problematic the position held by the ECJ in ACT Group Litigation case (Chapter 3) in favour of LOB clause because it undermines the compatibility between the EU fundamental freedoms and the measures provided by Action 6 of the BEPS Project.

The author considers the LOB clause (alone or in combination with the PPT clause) compatible with EU fundamental freedoms only when MFN treatment applies.

In conclusion (Chapter 4), the author finds that an EU MFN treatment principle, beyond preserving the neutrality of the Internal Market, would reconcile the actual clash between EU law and Action 6 BEPS' anti-abuse rules (LOB and PPT clauses) because it would correct the «mismatching effect» of the Action 6 BEPS' implementation in the EU when it is capable of harming harm «non-wholly artificial» arrangement.

D. case argument for saving the LOB clause; 2.1.3. Weaknesses of the ECJ's approach to MFN treatment: a gateway for tax treaty «competition»; 2.2. A new principle of equality for EU law: effects on fundamental freedoms; 2.2.1. A «substantial» EU principle of equality for the Internal Market neutrality; 2.2.2. A more consistent «comparability test»; 2.2.3. MFN treatment principle to avoid the breach of the fundamental freedoms; 2.3. The re-evaluation of the anti-abuse justification in the «rule of reason» doctrine; 2.3.1. The anti-abuse justification in ECJ case law; 2.3.2. The new role of the anti-abuse justification against treaty shopping; 2.3.3. Effects on EU and non-EU «investors»; 2.3.4. The proportionality test; 3. Compatibility of EU anti-abuse justification approach with Action 6 BEPS; 3.1. Actual discrepancies between EU law and Action 6 BEPS; 3.2. Compatibility of the EU MFN treatment with the Action 6 BEPS; 3.2.1. The anti-abuse justification in line with the Action 6 BEPS; 3.2.2. EU MFN treatment: a step forward; 4. Conclusions.

1. Introduction

Most Favoured Nation (hereinafter «MFN») treatment concept is closely connected with the non-discrimination principle since it implies that source country cannot subject an inbound investment to different treatment according to the origin of the investors, ultimately with regards their residence.

The ECJ ruled that EU law does not provides a general MFN treatment principle, arguing that when a source state (Member State) grants a more favoured tax treaty benefit to a resident of a Member State compared to the treatment granted to a resident of another Member State (*D*. case) there is no «horizontal discrimination» because taxpayers resident in different «contracting» states are not in comparable circumstances. That position of ECJ can be found not consistent with the fundamental freedom of the Internal Market because taxpayers in a factual and legal comparable situation are treated differently.

For the same reasons, the ECJ rejected the «horizontal discrimination» related to the application of the LOB clause (*Class IV ACT* case). The ECJ's approach can create compatibility problems between EU law and the LOB clause introduced by Action 6 of the BEPS Project. The fact that the new LOB clause, at a certain extent, will not address only «wholly artificial arrangement», but also «genuine economic activities», can breach the free-

dom of establishment principle provided by art. 49 of the TFEU (*Cadbury Schweppes* case).

New insights are offered by the recent ECJ's «Danish cases», where the Court adopted an «interposition approach» to defuse the application of DTC when the Parent-Subsidiary and Interest-Royalties Directive's benefits should be denied because the recipient of the payment is a «conduit» company.

The purpose of this paper is leading a journey through the inconsistencies of the ECJ's cases on MFN and LOB. Those contradictions will be the basis to research more a consistent principle of equality to achieve the neutrality of the Internal Market. The effect of this new approach will be assessed in the «comparability tests» (for non-discrimination purposes) to verify the condition for the recognition of an EU MFN treatment principle. The compatibility of this principle will be tested against the anti-abuse clauses (LOB and PPT) provided by Action 6 of the BEPS Project. Finally, it will be established whether the introduction of an MFN principle is the best choice for the internal and external consistency of the Internal Market.

2. EU MFN treatment against Treaty Shopping and the anti-abuse justification «antidote»

2.1. The current ECJ's approach to MFN and LOB

2.1.1. ECJ cases on MFN in direct taxation

The ECJ refuses the principle of MFN treatment in the field of direct taxation when the benefit to be extended form integral part of a DTC, because the extension of such advantages are considered to affect the «allocation» of taxing rights between source and resident state that cannot be undermined by EU law.

In particular, the dubious is if EU law requires Member States to apply a principle of MFN treatment to pursue the Internal Market neutrality and to avoid the infringement of the fundamental freedoms. The ECJ has already addressed this problem in different contexts. ECJ accepted the principle of MFN treatment in its general cases[1]. Different conclusion the

[1] ECJ's general case law recognizes an EU principle of MFN treatment regarding different

Court reached in the field of direct taxation. As we will see, the ECJ's approach to the MFN treatment principle direct taxation depends on the existence of a double tax convention (later also «DTC») that attribute the advantage to be extended[2].

In *Gilly* case[3], the ECJ decided about the situation of Mrs Gilly, a German and French citizen, that lived in France with her family but used to work in Germany. According to the DTC Germany-France, Mrs Gilly's employment income was taxed in Germany while France should grant her an ordinary tax credit. The taxpayer complained about the fact that, because the German tax scale had a more progressive effect than the French one, she could not get in France the credit for the full amount of tax paid in Germany, so that she remained subject to double taxation. The ECJ rejected the argument of the discrimination considering that, on the one hand, the allocation of taxing right through DTC is in the exclusive competence of Member States and, on the other hand, as the exercise by Member States of their taxing right can arise some «disparities», meaning that tax levied in one state can result higher than the ones levied in the second state. Because of lack of direct tax «harmonisation» in EU, the disadvantage suffered by Mrs Gilly was judged as the simple effect the simultaneous exercise of France and Germany's tax sovereignty and, for that reason, was not capable of triggering a breach of the fundamental freedoms[4].

fundamental freedoms. In case law about the free movement of goods ECJ found out that, as a general rule, a host state cannot treat imports differently according their state of origin, although EU law allows Member States (*Roders* case) to reach further integration between them, because the national treatment (*Kortmann* case) should apply for all imports, unless there are exceptions provided by EU Treaties or an authorization by the Commission (*Italy v. Commission* case). In the context of free movement of persons the ECJ requires Member States to extend to resident non-national the MFN treatment provided by their treaty network (*Matteucci* case). In the area of social security - after a first decision in favor of the prevalence of bilateral treaties over EU law (*Grana Novoa* case) - the Court reached the conclusion that EU law has replaced treaties between Member States so the latter should be now implemented according to EU law (*Gottardo* case) in the way that Member States are obliged to grant to non-nationals the social security advantages that their nationals already benefit based on social security agreement with third states.

2 M. Lang - J. Schuch - C. Staringer, *Tax treaty law and EC law*, Wien, Linde, 2007, 115-119.

3 Court of Justice, Judgment 12 May 1998, Case C-336/96, *Mr and Mrs Robert Gilly v Directeur des services fiscaux du Bas-Rhin*, ECLI:EU:C:1998:221.

4 Court of Justice, Judgment 12 May 1998, Case C-336/96, *Mr and Mrs Robert Gilly v Directeur des services fiscaux du Bas-Rhin*, ECR I- ECLI:EU:C:1998:221, para. 44, 46, 47 and 48.

The ECJ showed in *Saint Gobain* case[5] to take into account the Member State's limits in the exercise of their tax sovereignty where DTC is involved. It was a situation in which a French company's permanent establishment in Germany had no access to the German participation exemption that was, instead, benefit from a German resident company. The Court considered the failure of Germany to extend the participation exemption regime to the French permanent establishment discrimination in breach of the freedom of establishment[6]. According to the Court, the fact that Member States can sign DTC to «allocate» their taxing right does not allow them to infringe the EU law's obligations. Besides, Germany's «unilateral extension» of domestic benefits was not considered a violation of the «allocation» of taxing right «reciprocally» agreed in DTC.

The Court addressed in a more direct way the MFN problem in *D.* case[7], in which the Court found out that a German resident owning a house in the Netherlands, constituting the 10% of his whole wealth (with a remaining 90% in Germany), should be considered in a different situation (with regard wealth tax for immovable property situated in the Netherlands) compared to a Belgium resident in the same factual circumstances that, unlike the first taxpayer, is not subject to Dutch wealth tax as the effect of the application of the DTC between the Netherland and Belgium[8]. Mainly, the allocation of taxing right agreed by the Member States through DTC was considered to involve «reciprocal» right and obligation, forming the overall right balance to which also belong special tax benefits. A resident of the contracting states that qualify for treaty benefit was considered in a different position than a taxpayer not addressed by the same treaty benefits[9]. Then in *D.* case, the ECJ excluded the discrimination and the breach of the fundamental freedoms because of the failure of the «comparability

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[5] Court of Justice, Judgment 21 September 1999, Case C-307/97, *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt*, ECLI:EU:C:1999:438.

[6] Court of Justice, Judgment 21 September 1999, Case C-307/97, *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt*, ECLI:EU:C:1999:438, para. 56, 57 and 63.

[7] Court of Justice, Judgment 5 July 2005, Case C-376/03, *D. v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, ECLI:EU:C:2005:424.

[8] J. Korving, *Internal market neutrality*, The Hague, Sdu, 2019, 256.

[9] Court of Justice, Judgment 5 July 2005, Case C-376/03, *D. v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, ECLI:EU:C:2005:424, para. 60, 61 and 62.

test». In *Riskin and Timmermans* case[10] the ECJ reached the same conclusion about third countries.

The recent *Sopora* case[11] also involves the MFN issue, although related to unilateral domestic benefit. The ECJ found that a domestic law, such as the Dutch law involved, that granted a more favourable treatment (30% of wage tax exemption) to employees (with particular skills) residing (for more than 16 out of 24 months before to work in the Netherlands) further than 150 km from the Netherlands borders should be considered in breach of the freedom of movement of workers[12]. In other words, the Court held that by treating differently non-residents leaving outside the 150 km distance area compared to the one living inside that perimeter, the unilateral domestic measure gave place to «horizontal discrimination»[13].

Thus, in «horizontal» comparable situation (non-resident and non-resident) the Court gives particular importance to the source of the different treatment, assuming that discrimination can be triggered only by a «unilateral» measure (*Sopora* case), but not even by a benefit connected with a tax treaty (*D.* cases), unless there is a «disparity» of exercise of Member States' taxing right (*Gilly* case)[14]. However, the Court found that in the «vertical» comparison situations (resident and non-resident), the argument of the existence of a DTC does not avoid discrimination (*Saint Gobain* case).

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[10] Court of Justice, Judgment 30 June 2016, Case C-176/15, *Guy Riskin and Geneviève Timmermans v État belge*, ECLI:EU:C:2016:488, para. 31 («In the context of bilateral tax conventions, it follows from the case-law of the Court that the scope of such a convention is limited to the natural or legal persons defined by it. Likewise, the benefits granted by it are an integral part of all the rules under the convention and contribute to the overall balance of mutual relations between the two contracting states (see, to that effect, judgments of 5 July 2005 in D., C-376/03, EU:C:2005:424, paragraphs 54 and 61 to 62, and of 20 May 2008 in Orange European Smallcap Fund, C-194/06, EU:C:2008:289, paragraphs 50 to 51). It must be noted, as the Advocate General did at point 43 of her Opinion, that that situation is the same with regard to double taxation conventions concluded with Member States or with third states»).

[11] Court of Justice, Judgment 24 February 2015, Case C-512/13, *C. G. Sopora v. Staatssecretaris van Financiën,* ECLI:EU:C:2015:108.

[12] Court of Justice, Judgment 24 February 2015, Case C-512/13, *C. G. Sopora v. Staatssecretaris van Financiën*, ECLI:EU:C:2015:108, para. 30, 32, 34 and 35.

[13] G. Meussen, *Horizontal Discrimination and EU law: the Sopora Case*, in *European taxation*, 2014, 324.

[14] E. Kemmeren, *Sopora: a Wellcome Landmark Decision on Horizontal Comparison*, in *EC tax review*, 2015, 180.

2.1.2. The ECJ's D. case argument for saving the LOB clause

The ECJ's «non-comparability» approach to the MFN was also used to justify the compatibility of the LOB clause with EU law in the *ACT Group Litigation* case[15].

In *ACT Group Litigation* case[16], United Kingdom denied tax credit (against economic double taxation) on dividend distributed by a resident company to a non-resident company, in application of a LOB clause (included in DTC between the Netherlands and the United Kingdom), being the latter company owned by a company resident in a third state with which the United Kingdom had not a DTC granting the same kind of aforesaid tax credit, while other companies benefited from such tax credit because this was also provided by DTC concluded by their shareholders' resident countries with the United Kingdom. Leveraging on the same argument used in *D*. case, the ECJ found that «[…] a company resident in a Member State which has concluded a DTC with the United Kingdom which does not provide for such a tax credit is not in the same situation as a company resident in a Member State which has concluded a DTC which does provide for one», since «the grant of a tax credit to a non-resident company receiving dividends from a resident company, as provided for under a number of DTCs concluded by the United Kingdom, cannot be regarded as a benefit separate from the remainder of those DTCs, but is integral part of them and contributes to their overall balance»[17].

The conclusion was that companies resident in the same state receiving foreign dividends are not in a comparable situation when their shareholders are resident in different counties, and this circumstance determines the application of different tax treaty benefits. The different treatment was not considered discrimination in breach of fundamental freedoms for the non-resident companies not entitled to that treaty benefit[18].

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[15] Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue ECLI:EU:C:2006:773.

[16] Case C-374/04 Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue ECLI:EU:C:2006:773.

[17] Court of Justice, Judgment 12 December 2006, Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue*, ECLI:EU:C:2006:773, para. 88 and 91.

[18] F. Debelva - D. Scornos - J. Van den Berghen - P. Van Braband, *op. cit.*, p. 135.

2.1.3. Weaknesses of the ECJ's approach to MFN treatment: a gateway for tax treaty «competition»

The ECJ's approach to MFN treatment is erroneous because of its «tautologic» reasoning, the muddle of the taxpayer's factual and legal situation with his «entitlement» to DTC's benefits and the confusion between «allocation» and «exercise» of taxing right when source state «unilaterally extend» its «domestic treatment» to a non-resident. Implicitly the Court recognizes the Member States' freedom of tax treaty «competition» that is capable undermining the Internal Market neutrality.

More in details, the approach of the ECJ to MFN treatment is not consistent, and the weakness of its reasoning become manifest in *D*. case, where the Court could not avoid addressing the issue of the MFN treatment in connection with DTC provisions. It seems that the ECJ worries that, where DTC provisions are involved, the implementation of the principle of non-discrimination in the «horizontal» situation would undermine the power of Member State to exercise their fiscal sovereignty in the relation of the other states. Therefore, the consolidation of such principle of «horizontal non-discrimination» is considered capable of making ineffective the Member States' DTC network.

Before to address the juridical aspects of the decision, it appears that the ECJ's reasoning in *D*. case is not consistent from a logical point of view, resulting in a «tautology» (or «circular argument») [19], since the premise of its argument includes already the conclusion. In the Court's decision, the circumstance that two non-resident taxpayers are treated differently because they are not covered by the same DTC constitutes both the premise (that arises the discrimination issue) and the reason for the conclusion of non-discrimination (derived by non-comparability of the two situations). Then, the «cause» of the discrimination (the different treatment of similar), instead of being challenged became directly the «reason» that excludes such discrimination.

Moving towards the «discrimination analysis» lead by the ECJ, this appears to confuse the «legal and factual situation» of the taxpayer (that constitute the base of the «comparability test») with the taxpayer's «entitlement» to DTC benefits (that instead constitute the «object» of the «discrimination analysis»)[20]. In fact, in the «comparability test», the Court takes

[19] J. Korving, *op. cit.*, p. 264.

[20] M.C. Pimentel, *D'istorsion of the Common Market? Analysis and Future Perspectives of the*

into account only the taxpayer's «entitlement» to DTC benefits and, paradoxically, exclude the legal and factual aspects, the only ones that should be included in such test[21]. Since the difference in the taxpayers' «entitlement» to DTC benefits become already part of the «compatibility test», it follows that the «discrimination analysis» has no object, because nothing anymore remains to be challenged. Then the «discrimination analysis» is only «apparent», because it does not perform any function.

The Court also held that a benefit provided by a DTC constitute an integral part of the reciprocal right and obligation agreed in the states' allocation of their taxing right, hence that treatment cannot be extended to a resident of a Member State which is not part of the same DTC[22]. In this part, the ECJ makes several mistakes. It is useful to remind that the purpose of DTC is to eliminate the double taxation, at the same time avoiding opportunities for double non-taxation, tax evasion or tax avoidance[23]. To achieve this purpose DTCs contains rules providing «allocation» of taxing rights between the countries involved, precisely through the «distributive rules» included in the articles 6-22 of DTC. These «distributive rules», being only «allocative» of the taxing power, are not capable creating taxing rights but can only «restrict» the application of internal law[24] in the way to «compress» the states' taxing right. Taxing rights belong to a state even when they are not exercised because states have the discretion to exercise it in future. On the contrary, some scholars think that the fact that in *D.* case, a Belgium resident was not taxed as the effect of DTC's allowance, divert this measure from the objective of avoiding double taxation[25]. In the author's opinion, countries can agree to restrict their «potential» taxing

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MFN Clause Within EC Law, in *Intertax*, 2006, 488.

[21] The Court considers Mr D. and a Belgium resident in a different situation because only the latter is entitled to the benefit provided by the Netherlands – Belgium DTC.

[22] Court of Justice, Judgment 5 July 2005, Case C-376/03, *D. v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen*, ECLI:EU:C:2005:424, para. 58, 61, 62 and 63.

[23] Preamble to the OECD MC.

[24] J.F. Avery Jone and AA.VV., *Liber Amicorum Luc Hinnerkens*, Bruxelles, Bruylant, 2002, 588.

[25] D. Weber, *The influence of European Law on direct taxation: recent and future developments*, Alphen aan den Rijn, Kluwer Law International, 2007, 100. D. Weber, *Most-Favoured-Nation Treatment under Tax Treaties Rejected in the European Community: Background and Analysis of the D Case*, in *Intertax*, 2005, 443. S. van Thiel, *A Slip of the European Court in the D case (C-376/03): Denial of the Most-Favoured-Nation Treatment because of Absence of Similarity?*, in *Intertax*, 2005, 455.

right through DTC even though the latter is not actually exercised. Then in *D*. case, the Netherlands restricted its source state's right to tax the immovable property of Belgium residents, through the DTC's allowance[26], and allocated that right to Belgium. The circumstance that Belgium did not exercise its taxing right on the immovable property held by its resident in the Netherlands does not mean that the provision above had not the purpose of avoiding double taxation, because one day Belgium could freely decide to tax.

That clarification brings us to affirm that in *D*. case the ECJ miss the opportunity to make a distinction between «allocation» of taxing right and «exercise» of taxing right. The «allocation» («if») of taxing right is agreed in DTC, instead of taxing rights are «exercised» («how») through domestic law also when are «restricted» by tax treaties[27]. Then in *D*. case, the equal treatment of Belgium and German's residents would have been the effect of the Netherlands's domestic law application (as restricted by DTC) and not the effect of the direct «extension» of the Netherlands-Belgium DTC to German resident (as wrongly hold by ECJ). Since DTC does not «create» taxing right, it is only the «domestic treatment» to be extended to another taxpayer through the similar «exercise» of taxing right. It follows that *D*. case does not even involve conflict between EU law and DTC because the only rule that should be extended to another non-resident taxpayer was the «restricted» domestic rule and not the DTC's provision. In other words, EU law requested to the Netherlands to «exercise» its taxing right in the same way for German's residents and Belgium's residents, without claiming the Netherlands to change the «allocation» of taxing right agreed in the Netherlands-Belgium DTC. The «unilateral extension» of such domestic treatment to a Germany's resident does not affect at all the Netherlands-Belgium DTC (this treaty does not apply to German's residents because it has only effect on residents of the contracting states). This constitutes application of the ECJ's reasoning in Saint-Gobain, «since such an extension would not in any way affect the rights of the non-member countries which are parties to the treaties and would not impose any new obligation on

[26] With regard to D. case it must be emphasized that the Netherlands-Belgium DTC's allowance constitute a «restriction» of the Netherlands' domestic law providing the general rule of taxation of the immovable property belonging to non-residents.

[27] A. Cordewener - E. Reimer, *The Future of Most-Favoured-Nation Treatment in EC Tax Law – Did the ECJ Pull the Emergency Brake without Real Need? – Part 2*, in *European taxation*, 2006, 300.

them»[28] with the effect that «As far as the exercise of the power of taxation so allocated is concerned, the Member States nevertheless may not disregard Community rules. According to the settled case-law of the Court, although direct taxation is a matter for the Member States, they must nevertheless exercise their taxation powers consistently with Community law»[2930]. This conclusion remain also true in relation to *ACT Group Litigation* case, since the application of a LOB clause «defuse» the taxpayer's DTC benefits, leaving the source state «unrestricted» (out of the «allocation» of taxing right agreed in DTC) in the exercise of its taxing right towards a non-resident compared to another non-resident for which the exercise of taxing right is still «restricted» by the same DTC. Hence, the different exercise of taxing rights for taxpayers in similar circumstances should be considered a discriminatory treatment.

EU law requires the Member States to «exercise» their taxing rights in the same manner for non-residents investors when fundamental freedoms are involved, and that extension cannot create any conflict with DTC that, instead, relate to «bilateral allocation» of taxing right. In the author's view, the departure of the ECJ from this approach creates more problems than those it wanted to solve, because in doing that the Court recognizes the Member States' freedom of tax treaty «competition». Member States can exercise their taxing rights and (then) give different benefit to foreign investors according to their state of residence, by merely «shield» that measures in DTC[31]. Because tax benefit gives some investors a competitive advantage

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[28] Court of Justice, Judgment 21 September 1999, Case C-307/97, *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt,* ECLI:EU:C:1999:438, para. 59.

[29] Court of Justice, Judgment 21 September 1999, Case C-307/97, *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt,* ECLI:EU:C:1999:438, para. 57.

[30] A. Cordewener - E. Reimer, *The Future of Most-Favoured-Nation Treatment in EC Tax Law – Did the ECJ Pull the Emergency Brake without Real Need? – Part 1*, in *European taxation*, 2006, 305.

[31] S. van Thiel, *A Slip of the European Court in the D case (C-376/03): Denial of the Most-Favoured-Nation Treatment because of Absence of Similarity?*, in *Intertax*, 2005, 455-456 («As regards the free movement of goods, Member states are for instance still competent to set mandatory environmental standards and they can also set the standard VAT rate as long as they respect the minimum of 15 per cent. According to the logic of the D. decision, a Member State such as the Netherlands could in a first step set certain maximum CO2 emission levels for imported cars or a minimum VAT rate of 18 per cent for intra-Community acquisitions, and subsequently in a second step agree bilaterally with one other Member State, for instance Belgium, to apply lower maximum CO2 emission levels for cars imported from Belgium and to set a 16 per cent VAT rate for intra Community acquisitions from Belgium»). D. Weber, *The influence of European Law on direct taxation: recent and future developments*, Alphen aan den

compared to others, the ECJ position undermines the EU principle of Internal Market neutrality[32]. In conclusion, the ECJ show to take more care about the «interest» of Member States than the «freedoms» of their citizen and residents[33].

2.2. A new principle of equality for EU law: effects on fundamental freedoms

2.2.1. A «substantial» EU principle of equality for the Internal Market neutrality

In order to achieve the neutrality of the Internal Market, EU law requires a «substantial» principle of equality according to which «horizontal discrimination» and «vertical discrimination» should receive the same disapproval regardless the existence of a tax treaty.

The essential characteristic of the EU Internal Market is the «neutrality», according to which the rules of the market should govern the economy without the intervention of the Member States that can treat to distort the competition[34]. The market competition can be distorted when operators in comparable situations are treated in different ways by the Member States, with the effect that someone is treated better than others are. In the author opinion, the achievement of «neutral» market depends on the «equality» treatment of operator acting in the «game» of the competition. The other side of the coin of «equality» is the non-discrimination rules. The main principle of non-discrimination can be found in art. 18 TFEU that prohibits discrimination on the base of nationality. That principle only applies if no other specific principle applies. Underlying non-discrimination rules are incorporated in other articles of TFEU dealing with the following economic «fundamental freedoms»: free movement of goods (art. 34 and 35 TFEU), freedom of movement of workers (art. 45 TFEU), freedom of establishment (art. 49 TFEU) and free movement of capital (art. 63 TFEU)[35].

Rijn, Kluwer Law International, 2007, 104.

[32] D. Weber, *Most-Favoured-Nation Treatment under Tax Treaties Rejected in the European Community: Background and Analysis of the D Case*, in *Intertax*, 2005, 400.

[33] H. van den Hurk - J. Korving, *The "D" Case against the Netherlands and the ECJ's Decision – Is There Still a Future for MFN Treatment?*, in *Bulletin – Tax Treaty Monitor*, 2006, 371.

[34] J. Korving, *op. cit.*, p. 122.

[35] R.S. Avi-Yonah - J.R. Hines - M. Lang, *Comparative fiscal federalism: comparing the European Court of Justice and the US Supreme Court's tax jurisprudence,* London, Kluwer Law

In the field of direct taxation, the ECJ conduct the «discrimination analysis» according to the following steps:

- Comparability test: does the domestic measure *ictu oculi* treat differently cross-border situation and internal situations (*prima facie* comparability test)? If that is the case, are there some objective differences between the two situations that make the distinction reasonable (teleological comparability test)?

- Justification test: can reasons of public interest justify the discrimination?

- Proportionality test: is the justified discrimination «effective» (appropriateness test) and restrict the free movement beyond what is «necessary» to achieve a legitimate scope (proportionality *stricto sensu* test)?[36]

In the author's opinion, ECJ's choice to applicate the non-discrimination rule only in case of «vertical discrimination»[37] (resident v. non-resident) but not in situation of «horizontal discrimination»[38] (non-resident v. non-resident), besides resulting in the aforementioned inconsistency and contradictions, derive from an erroneous formulation of the principle of equality with regards to the scope of neutrality of Internal Market. It is inadmissible the ECJ's argument according to which a different treatment of two non-residents in the same factual situation can trigger a discriminatory treatment as long as the measure is not provided by a DTC. As we have seen before, both in the presence and in the absence of «allocation» of taxing rights between the Member States through DTC, only the «exercise» of the source State's (limited or not limited by DTC) taxing right is capable to trigger the discrimination of investors according to their states of residences. The different «exercise» of taxing right for taxpayers in similar legal and factual situation constitute discrimination both in «horizontal comparison» and in «vertical comparison», as a violation of the principle of equal treatment, because only in that sense the principle of equality is strictly functional to achieve the Internal Market neutrality. In fact, while the «allocation» of taxing right produces effects between states («balancing» their fiscal power), the «exercise» taxing power affects the position of

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International, 2007, 48.

[36] P.J. Wattel - O. Marres - H. Verneulen, *Terra/Wattel European Tax Law*, Deventer, Kluwer, 2018, 41-42.

[37] Court of Justice, Judgment 24 February 2015, Case C-512/13, *C. G. Sopora v. Staatssecretaris van Financiën*, ECLI:EU:C:2015:108, para. 30, 32, 34 and 35.

[38] Court of Justice, Judgment 5 July 2005, Case C-376/03, *D. v Inspecteur van de Belastingdienst/ Particulieren/Ondernemingen buitenland te Heerlen,* ECLI:EU:C:2005:424, para. 60, 61 and 62.

taxpayers, resulting in higher or lower tax burden. This tax burden, like an economical cost, can create «inequality» between taxpayers, resulting in discriminatory treatment in breach of the fundamental freedoms.

The fact Member States should comply with this such principle of equality would not undermine their fiscal sovereignty (e.g. «harmonisation» of direct taxation), because they are still capable of establishing the tax policy adequate to achieve the target tax revenue. The power of a Member State to decide how «exercise» its taxing right according to the residence of the foreign investors through DTCs concern tax treaty «competition» policy and not also tax revenue policy. The proposed principle of equality would only be incompatible with the Member States' tax treaty «competition» and not with their tax revenue policy (that constitute the highest expression of a State's fiscal sovereignty). For example, Member States would still decide the minimum amount of withholding to apply to dividends and interests (art. 10 and 11 of the signed DTC), according to their tax revenue needs. On the other side, the Member States' power of implementing a tax treaty «competition» is neither request by DTC's scope of avoiding double taxation. Equal source state's treatment can easily correspond to equal double tax relief granted by the resident state. There is no pressing reason to sacrifice such equality principle and the neutrality of Internal Market in favour of Member States' freedom of tax treaty «competition».

Looking at ECJ's «state aid» decisions, it's sustainable that the proposed «substantial» principle equality is also implied by the existence of an EU arm's length principle in the contest of the intra-group transaction. In *Forum 187 ASBL* case[39] ECJ clarified that in EU law a general arm's length principle is in force with whom the Member States should comply to avoid distortion of competition in Internal Market[40]. In the author view, it is enough to affirm the existence of the proposed «substantial» EU principle of equality that every Member State should respect. Ban on «state aid»

[39] Court of Justice, Judgment 22 June 2006, Joined Cases C-182/03 and C-217/03, *Kingdom of Belgium and Forum 187 ASBL v Commission of the European Communities*, ECLI:EU:C:2006:416.

[40] Court of Justice, Judgment 22 June 2006, Joined Cases C-182/03 and C-217/03, *Kingdom of Belgium and Forum 187 ASBL v Commission of the European Communities*, ECLI:EU:C:2006:416, para. 95 («In order to decide whether a method of assessment of taxable income such as that laid down under the regime for coordination centres confers an advantage on them, it is necessary, as the Commission suggests at point 95 of the contested decision, to compare that regime with the ordinary tax system, based on the difference between profits and outgoings of an undertaking carrying on its activities in conditions of free competition»).

and fundamental freedoms protection are two faces of the same principle of equality. There is no reason to hold that only in «state aid» cases the Internal Market neutrality cannot be frustrating by formalistic elements. The only difference between «state aid» and fundamental freedoms' rules is that only the first ones are applied by ECJ both in the cross-border and domestic situations, instead fundamental freedoms are usually applied only in a cross-border situation. However, that difference does not affect the application of the proposed «substantial» EU principle of equality in the «horizontal comparison» context because this scenario involves two cross-border situations.

From a more practical point of view, the need for a «substantial» EU principle of equality to achieve the Internal Market neutrality is even more evident in situations in which, for example, freedom of movement of capital is involved, because the modern faster, more comfortable and lower cost-shifting of capital create more opportunities for distortion of Internal Market functioning compared, for example, with the free movement of workers in which the economic dynamics are slower, more complicated and at higher cost. There is no reason to deny the application of this «substantial» EU principle of equality in a situation that can more probably undermine the neutrality of the Internal Market.

From a broader perspective, in giving relevance to the factual situation of taxpayer instead that his formal entitlement to treaty benefits[41], the proposed «substantial» principle of equality is also consistent with the «substance-over-form» approach of the OECD BEPS Project[42] and with the OECD fight against the «harmful tax competition»[43].

2.2.2. A more consistent «comparability test»

As the effect of the proposed «substantial» EU principle of equality, non-residents in a similar «personal» factual and legal situation (only from the perspective of the source state) should receive equal treatment according to the «comparability test» (in the context of the «discrimination analysis»).

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[41] Court of Justice, Judgment 5 July 2005, Case C-376/03, *D. v Inspecteur van de Belastingdienst/Particulieren/Ondernemingen buitenland te Heerlen,* ECLI:EU:C:2005:424, para. 60, 61 and 62.

[42] OECD*, OECD/G20 Base Erosion and Profit Shifting*, Paris, OECD, 2015, available at https://www.oecd.org/ctp/beps-2015-final-reports.htm.

[43] OECD, *Harmful Tax Competition*, Paris, OECD, 1998, available at https://read.oecd-ilibrary.org/taxation/harmful-tax-competition_9789264162945-en#page1.

To address correctly the «discrimination analysis» in «horizontal comparison», two non-resident investors from different foreign countries should be considered in comparable situation, from the perspective of the source state, because in both case the latter can «exercise» its taxing right in the limit of the taxable base located in its territory[44]. For example, this means that in *D*. case a Belgium and a German resident, having 10% of immovable property in the Netherlands, should receive the same tax treatment from the last states. That conclusion is also requested by the application of the *a contrario* reading of *Schumacker* case[45], according to which non-resident producing less than 90% of their income in the source state can be considered in comparable situation (because both non-residents fail the «Schumacker test»)[46]. The other way around, when both non-residents pass the Schumacker test, they are still in comparable situation («horizontal comparability»), but this time they are also comparable to residents of the source state («vertical comparability»). Considering *X* case[47], this last reasoning remains valid also when both non-residents fail the «Schumacker test» because they earn the entire income abroad but in different source

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[44] A. Cordewener - E. Reimer, *op. cit.*, p. 301.

[45] Court of Justice, Judgment 14 February 1995, Case C-279/93, *Finanzamt* Köln-Altstadt v Roland Schumacker, ECLI:EU:C:1995:31, para. 37 and 38.

[46] G.W. Kofler - C.P. Schindler, *Dancing with Mr D": The ECJ's Danial of Most-Favoured-Nation Treatment in the "D" case*, in *European taxation*, 2005, 538.

[47] Court of Justice, Judgment 9 February 2017, Case C-283/15, *X v Staatssecretaris van Financiën*, ECLI:EU:C:2017:102, para 47-48 («47. It follows, in particular, that the freedom of the Member States, in the absence of unifying or harmonising measures adopted under EU law, to allocate among themselves their powers to impose taxes, in particular to avoid the accumulation of tax advantages, must be reconciled with the necessity that taxpayers of the Member States concerned are assured that, ultimately, all their personal and family circumstances will be duly taken into account, irrespective of how the Member States concerned have allocated that obligation amongst themselves. Were such reconciliation not to take place, the freedom of Member States to allocate the power to impose taxes among themselves would be liable to create inequality of treatment of the taxpayers concerned which, since that inequality would not be the result of disparities between the provisions of national tax law, would be incompatible with freedom of establishment (see, to that effect, judgment 12 December 2013, Imfeld and Garcet, C-303/12, EU:C:2013:822, paragraphs 70 and 77). 48. In the situation where a self-employed person receives his taxable income within a number of Member States, other than that where he is resident, that reconciliation can be achieved only by permitting him to submit a claim for his right to deduct 'negative income' to each Member State of activity where that type of tax advantage is granted, in proportion to the share of his income received within each such Member State, it being his responsibility to provide to the competent national authorities all the information on his global income needed by them to determine that proportion»).

states, since also in this case they are in comparable situation[48]. In the author's opinion, also the application of a «pro-rata parte» approach[49] (currently not confirmed by the ECJ) would have no effect on the «comparability» of the taxpayers but on the measure of the benefits to be extended.

One can wonder if the resident state's «neutralization» of the source state's discriminatory measure (through double tax relief) should be taken in account to assess the similarity in both «vertical comparability» and «horizontal comparability» scenarios. The ECJ accepts the «double-country approach» when the «neutralization» is provided «unilaterally» by resident state and rejects it only when such «neutralization» is agreed in DTC[50]. In *Denkavit* and in *Amurta* cases the Court stated that only in the latter situation the obligation of the resident state to «neutralize» the discriminatory treatment became part of the source state's rules and link source state's and resident state tax systems in a way to comply with the EU's non-discrimination principle[51]. Nevertheless, some scholars argue that the unilateral «neutralization» is enough to exclude discrimination[52].

The author has a different opinion. Both the approach are unsustainable from a logical point of view before then a juridical one. The «comparability test» is the logical premise of the «discrimination analysis», so has no sense firstly wonder if a discriminatory treatment can be neutralized for the purpose of the «comparability test», otherwise the «discrimination analysis» will become itself the premises of the «comparability test». As we have seen in *D.* case, ECJ likes such circular reasoning in which the object becomes the premises of the analysis. From a juridical point of view, the comparison between different situations should be made from the perspective of source state's exercise of taxing right, because this is the object of the «discrimination

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[48] P.J. Wattel - O. Marres - H. Verneulen, *op. cit.*, p. 461.

[49] P.J. Wattel - O. Marres - H. Verneulen, *op. cit.*, p. 461.

[50] Court of Justice, Judgment 14 December 2006, Case C-170/05, *Denkavit Internationaal BV and Denkavit France SARL v Ministre de l'Économie, des Finances et de l'Industrie*, ECLI:EU:C:2006:783, para. 46-47; Court of Justice, Judgment 8 November 2007, Case C-379/05, *Amurta SGPS v Inspecteur van de Belastingdienst/Amsterdam*, ECLI:EU:C:2007:655, para. 83; Court of Justice, Judgment 12 December 2002, Case C-385/00, *F.W.L. de Groot v Staatssecretaris van Financiën*, ECLI:EU:C:2002:750, para. 100.

[51] G. Kofler, *European Union – Tax Treaty «Neutralization» of Source State Discrimination under the EU Foundamental Freedoms?*, in *Bulletin for International Taxation*, 2011, 106.

[52] E. Kemmeren, *ECJ should not unbundle integrated tax system!*, in *EC tax review*, 2008, 9. A. Cordewener - E. Reimer, *The Future of Most-Favoured-Nation Treatment in EC Tax Law – Did the ECJ Pull the Emergency Brake without Real Need? – Part 2*, in *European taxation*, 2006, 35.

analysis». Notably, a double tax relief provided by a DTC constitute a «restriction» of the taxing right of a resident state because from a practical point of view this cannot collect the entire amount of tax ordinarily due on the amount of income involved. That «exercise» of taxing right (although limited by DTC) is only «imputable» to the resident state. The same conclusion we can reach if the resident state's domestic law would unilaterally provide double tax relief. Given that the (limited) «exercise» of taxing right is only «imputable» to the resident state, it cannot be taking into account within the «discrimination test» of the source state's domestic law because the latter (for its part) is only «imputable» to the exercise of source state's taxing rights. In other words, the discriminatory treatment «imputable» to the source state's «exercise» of its taxing right (through its domestic law) cannot be found depending on the «exercise» of taxing right «imputable» to the resident state[53][54].

Under a different profile, the «comparability test» should take in consideration only the taxpayer's «personal» situation subjected to the «discrimination analysis», without taking into account other taxpayers' «personal position» (connected or not connected to the first taxpayer). In other words, a « single» taxpayer «discrimination analysis» cannot start from a taxpayers «group» based «comparability test»[55].

2.2.3. MFN treatment principle to avoid the breach of the fundamental freedoms

An EU MFN treatment principle would grant to non-residents in comparable situation same «tax treaty» benefits avoiding the «horizontal dis-

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[53] Although this conclusion is not in line with the ECJ's position on the source state's discrimination «neutralization» effect, it finds support in some ECJ cases regarding double juridical taxation: Court of Justice, Judgment 12 May 1998, Case C-336/96, *Mr and Mrs Robert Gilly v Directeur des services fiscaux du Bas-Rhin*, ECR I- ECLI:EU:C:1998:221; Court of Justice, Judgment 14 November 2006, Case C-513/04, *Mark Kerckhaert and Bernadette Morres v Belgische Staat*, ECLI:EU:C:2006:713; Court of Justice, Judgment 12 February 2009, Case C-67/08, *Margarete Block v Finanzamt Kaufbeuren*, ECLI:EU:C:2009:92; Court of Justice, Judgment 4 February 2016, Case C-194/15, *Véronique Baudinet and Others v Agenzia delle Entrate - Direzione Provinciale I di Torino*, ECLI:EU:C:2016:81.

[54] J. Schuch, *Most favoured nation clause' in the Tax Treaty Law*, in *EC tax review*, 1996, 165. F.P. Sutter - U. Zehetner, *Triangular tax cases*, Wien, Linde, 2004, 462-463.

[55] Court of Justice, Judgment 12 December 2006, Case C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue*, ECLI:EU:C:2006:773, para. 91. Breaking this logic principle, ECJ argued that two non-resident receiving dividend can be treated differently by the source state according to the residence of their respective shareholders because on this element depends the application of the DTC's LOB clause.

crimination» in breach of the fundamental freedoms in the field of direct taxation.

The proposed «comparability test» implies as a rule that a Member State cannot differentiate the treatment of inbound investments according to the residence the investors in a similar («personal») factual and legal situation. When it involves fundamental freedoms, the infringement of the non-discrimination principle results in a «horizontal discrimination» because non-residents in comparable situations have no access to the same benefits. It follows that the source state is obliged to grants the MFN treatment to foreign investors to avoid the breach of the fundamental freedoms involved. In this case, the principle of non-discrimination would apply for both EU and non-EU investors in relation to the freedom of movement of capital (art. 63-66 TFEU) and only for EU individuals and undertaking about the freedom of establishment (art. 49-53 TFEU). Moreover, when non-residents in «comparable» situation are also in a position similar to the source state's residents, beyond granting to non-residents equal tax treatment («MFN treatment») the source state should also treat them (according *Schumacker* case and *X* case) not «less favourable» than its own residents («vertical non-discrimination»). The same reasoning applies for outbound dividends, interest and royalties[56], for which source state should ensure that non-residents do not pay more taxes than residents do[57]. Only at that extent, it is possible to affirm that resident and non-residents undertaking compete in a neutral Internal Market.

The implementation of the MFN treatment principle into EU Internal Market will have the advantage to stop treaty shopping inside EU laid by (at least) Member States' residents because the latter would have no reason to set-up an «intermediary» or «conduit» company in a different Mem-

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[56] Court of Justice, Judgment 12 June 2003, Case C-234/01, *Arnoud Gerritse v Finanzamt Neukölln-Nord*, ECLI:EU:C:2003:340; Court of Justice, Judgment 9 November 2006, Case C-520/04, *Pirkko Marjatta Turpeinen*, ECLI:EU:C:2006:703; Court of Justice, Judgment 3 October 2006, Case C-290/04, *FKP Scorpio Konzertproduktionen GmbH v Finanzamt Hamburg-Eimsbüttel*, ECLI:EU:C:2006:630; Court of Justice, Judgment 15 February 2007, Case C-345/04, *Equestre da Lezíria Grande Lda v Bundesamt für Finanzen*, ECLI:EU:C:2007:96; Court of Justice, Judgment 22 December 2008, Case C-282/07, *Belgian State - SPF Finances v Truck Center SA*, ECLI:EU:C:2008:762; Court of Justice, Judgment 18 October 2012, Case C-498/10, *X NV v. Staatssecretaris van Financiën*, ECLI:EU:C:2012:635; Court of Justice, Judgment 17 September 2015, Joined Cases C-10/14, C-14/14 and C-17/14, *J. B. G. T. Miljoen, X, Société Générale SA v Staatssecretaris van Financiën*, ECLI:EU:C:2015:608.

[57] P.J. Wattel - O. Marres - H. Verneulen, *op. cit.*, p. 428.

ber State if the source state's treatment of inbound investment would not change according to the residence of the investors.

However, the simple application of such MFN treatment principle would allow some (EU and non-EU) investors to benefit from a better combined source-resident states tax treatment compared to the one applicable to other investors, as the effect of the different double tax relief rules applied by resident countries. Also, a problem would remain in the term of treaty shopping put in place by non-EU residents using EU resident «conduit» entities to take advantage of the EU MFN treatment. These problems cannot be solved at the level of «comparability test». Nevertheless, the fact that as a general rule, the source state must comply with the MFN treatment principle does not mean that discriminatory treatment of a non-resident is always in breach of fundamental freedoms. Reasons of public interest can still justify the «horizontal discriminatory» treatment according to the «justification test». In the author's opinion, elements that must be excluded from the «comparability test», because considered unrelated to the factual and legal condition of the taxpayer, can find their «natural» place into the «justification test» to assess if «discriminatory measures» can be «saved» by reasons of «public interest».

2.3. The re-evaluation of the anti-abuse justification in the «rule of reason» doctrine

2.3.1. The anti-abuse justification in ECJ case law

The ECJ accepts anti-abuse reasons as a justification of discriminatory treatment with some limitation related to the protection of the Internal Market neutrality and the taxpayer's right.

When discrimination is found, the next step is to assess if it can be justified. EU law codifies some justifications of the infringement of fundamental freedoms, with the scope to protect public order, public safety and public health. However, considering that it is unlikely that such justification is involved in direct taxation matters, ECJ has elaborated a series of other justifications for direct taxation issues related to imperative reasons of «public interest», named «rule of reasons». On this base, ECJ accepts the following justifications: effectiveness of fiscal supervision (when one country cannot realise what is happening in the other country because of the lack of exchange of information)[58]; balanced allocation of taxing

[58] Court of Justice, Judgment 10 April 2014, Case C-190/12, *Emerging Markets Series of DFA*

right (e.g. the application of the principle of territoriality can fulfil this justification[59]); coherence of tax system (the deny of benefit constitute a «direct linked» compensation for another advantage)[60]; avoid of double loss compensation (when the granting of loss compensation in one state would be added to a loss compensation in another state)[61]; prevention of tax avoidance (detected by domestic anti-abuse provisions)[62][63].

However, the ECJ accepts the anti-abuse justification as long as it has been implemented through a domestic law that does not include a general

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Investment Trust Company v. Dyrektor Izby Skarbowej w Bydgoszczy, ECLI:EU:C:2014:249, para. 71; Court of Justice, Judgment 23 January 2014, Case C-296/12, *European Commission v. Kingdom of Belgium*, ECLI:EU:C:2014:24, para. 42; Court of Justice, Judgment 9 October 2014, Case C-326/12, *Rita van Caster e Patrick van Caster v. Finanzamt Essen-Süd*, ECLI:EU:C:2014:2269, para. 46; Court of Justice, Judgment 19 June 2014, Case C-53/13, *Strojírny Prostějov, a.s. e ACO Industries Tábor s.r.o. v. Odvolací finanční* ředitelství, ECLI:EU:C:2014:201, para. 55.

[59] Court of Justice, Judgment 7 September 2006, Case C-470/04, *N v. Inspecteur van de Belastingdienst Oost/kantoor Almelo*, ECLI:EU:C:2006:525, para. 41; Court of Justice, Judgment 29 November 2011, Case C-371/10, *National Grid Indus BV v. Inspecteur van de Belastingdienst Rijnmond/kantoor Rotterdam*, ECLI:EU:C:2011:785, para. 45.

[60] Court of Justice, Judgment 10 April 2014, Case C-190/12, *Emerging Markets Series of DFA Investment Trust Company v. Dyrektor Izby Skarbowej w Bydgoszczy*, ECLI:EU:C:2014:249, para. 91; Court of Justice, Judgment 13 March 2014, Case C-375/12, *Margaretha Bouanich v. Directeur des services fiscaux de la Drôme*, ECLI:EU:C:2014:138, para. 69; Court of Justice, Judgment 12 June 2014, Case C-39/13, *Inspecteur van de Belastingdienst / Noord/kantoor Groningen e.a. v. SCA Group Holding BV e.a.*, ECLI:EU:C:2014:1758, para. 53; Court of Justice, Judgment 24 February 2015, Case C-559/13, *Finanzamt Dortmund-Unna v Josef Grünewald*, ECLI:EU:C:2015:109, para. 48.

[61] Court of Justice, Judgment 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:2005:763, para. 55.

[62] Court of Justice, Judgment 16 July 1998, Case C-264/96, *Imperial Chemical Industries plc (ICI) v Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:1998:370, para. 26; Court of Justice, Judgment 26 September 2000, Case C-478/98, *Commission of the European Communities v Kingdom of Belgium*, ECLI:EU:C:2000:497, para. 45; Court of Justice, Judgment 21 November 2002, Case C-436/00, *X and Y v. Riksskatteverket*, ECLI:EU:C:2002:704, para. 51; Court of Justice, Judgment 11 March 2004, Case C-9/02, *Hughes de Lasteyrie du Saillant v Ministère de l'Économie, des Finances et de l'Industrie*, ECLI:EU:C:2004:138, para. 51; Court of Justice, Judgment 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:2005:763, para. 49; Court of Justice, Judgment 12 September 2006, Case C-196/04, *Cadbury Schweppes plc e Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*, ECLI:EU:C:2006:544, para. 55; Court of Justice, Judgment 13 March 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue*, ECLI:EU:C:2007:161, para. 72; Court of Justice, Judgment 18 July 2007, Case C-231/05, *Oy AA.*, ECLI:EU:C:2007:439, para. 58.

[63] J. Korving, *op. cit.*, pp. 282-289.

presumption of abuse for cross-border operation[64], does not also address genuine construction[65] and, where providing a general anti-abuse principle, the taxpayer has the right to provide counter-evidence[66].

2.3.2. The new role of the anti-abuse justification against treaty shopping

Treaty shopping strategies not «defused» by the EU MFN treatment principle can be smashed by the «antidote» of the anti-abuse justification.

The EU MFN treatment as the application of the non-discrimination principle does not give an answer to the following problems:

- double non-taxation benefit for EU residents or non-EU residents as the combined effect of MFN treatment in (Member State) source state (e.g. 0% withholding tax) and double taxation relief in (Member State or non-EU country) resident state (e.g. exemption on foreign income);
- treaty shopping strategy performed by non-EU residents through «conduit» companies established in a Member State to benefit from a lower (Member State) source state's taxation.

In both the situations, the claim for the application of MFN treatment is «abusive», because it results in a non-taxation of the taxpayer's income. This means that the MFN treatment principle creates problems only when it operates for «abusive» purposes. For that reason, a violation of MFN treatment principle should be justified in «abusive» situation, while there is no reason to deny MFN treatment when an abusive situation is not in-

[64] Court of Justice, Judgment 16 July 1998, Case C-264/96, *Imperial Chemical Industries plc (ICI) v Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:1998:370, para. 26; Court of Justice, Judgment 21 November 2002, Case C-436/00*, X and Y v. Riksskatteverket*, ECLI:EU:C:2002:704, para. 51; Court of Justice, Judgment 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:2005:763, para. 49; Court of Justice, Judgment 13 March 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue*, ECLI:EU:C:2007:161, para. 72.

[65] Court of Justice, Judgment 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:2005:763, para. 4; Court of Justice, Judgment 12 September 2006, Case C-196/04, *Cadbury Schweppes plc e Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*, ECLI:EU:C:2006:544, para. 55; Court of Justice, Judgment 18 July 2007, Case C-231/05, *Oy AA.*, ECLI:EU:C:2007:439, para. 58.

[66] Court of Justice, Judgment 26 September 2000, Case C-478/98, *Commission of the European Communities v Kingdom of Belgium*, ECLI:EU:C:2000:497, para. 45; Court of Justice, Judgment 21 November 2002, Case C-436/00*, X and Y v. Riksskatteverket*, ECLI:EU:C:2002:704, para. 61; Court of Justice, Judgment 11 March 2004, Case C-9/02, *Hughes de Lasteyrie du Saillant v Ministère de l'Économie, des Finances et de l'Industrie*, ECLI:EU:C:2004:138, para. 51.

volved. While the ECJ denies MFN treatment application at the level of «comparability test», excluding the non-discriminatory treatment also in the «non-abusive» situation, in the author's opinion, the challenge of MFN treatment at «justification test» level would have the advantage to exclude that benefit only for anti-abuse reasons.

Now the problem is to identify which anti-abuse rule can justify the discrimination that violates the MFN treatment principle. Anti-abusive rules can be included both in domestic law and in DTC, so that three scenarios can occur:

- anti-abuse rules included in source state's domestic law but not included in DTC;
- anti-abuse rules included in DTC;
- anti-abuse rules included neither in source state's domestic law nor in DTC.

Anti-abuse rules included in source state's domestic law but not included in DTC

In the first scenario, in which only source state's domestic law provides for an anti-abuse rule, it is arguable that benefits of a DTC can still be granted, in consideration of the supremacy of DTC provisions compared to domestic law incompatible with the former. However, for this purpose, it is useful to remember that, while before 2003 revisions, the Commentary to art. 1 of OECD Model provided that scope of tax treaties was to facilitate international trade and eliminate international double taxation, in the Commentary to OECD Model 2003 was added: «It is also a purpose of tax conventions to prevent tax avoidance and evasion» (Sec. 7), with the result that «A guiding principle is that the benefits of a double taxation convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provisions» (Sec. 9.5). Regarding the relation between DTC and domestic law, it was specified that: «Such [anti-abuse] rules are part of the basic domestic rules set by domestic tax laws for determining which facts give rise to a tax liability; these rules are not addressed in tax treaties and are therefore not affected by them. Thus, as a general rule and having regard to paragraph 9.5, there will be no conflict. For example, to the extent that the application of the rules referred to

in paragraph 22 results in a recharacterisation of income or in a redetermination of the taxpayer who is considered to derive such income, the provisions of the Convention will be applied taking into account these changes» (Sec. 22.2)[67]. Moreover, the Commentary to art. 1 of OECD Model 2017 has been pointed out that, both in case of conflict between domestic SAAR (Specific legislative anti-abuse rules) or GAAR (General legislative anti-abuse rules) and tax treaty provisions, the «apparent» conflict can be avoided, because:

– in many cases the application of the domestic measures only have an impact on how the treaty provisions apply[68];
– that provision would be in line with the general scope of DTC to not grant its benefit where arrangements constitute an abuse contrary to the object and purpose of the relevant provisions[69].

It follows that domestic anti-abuse provisions having the scope to avoid treaty shopping cannot be found in conflict with DTC lucking of such anti-abuse measures[70].

Anti-abuse rules included in DTC

When anti-abuse rules are included in DTC (under paragraph 9 of art. 29 (PPT)), according to Commentary to art. 1 of OECD Model 2017 there is no conflict with domestic SAAR or the GAAR if these apply in the same circumstances in which the benefit of the treaty would be denied under that treaty's provision[71][72].

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[67] OECD MC Comm. 2003 on Art. 1, available on: https://www.oecd-ilibrary.org/docserver/mtc_cond-2003-en.pdf?expires=1563100370&id=id&accname=oid048188&checksum=535C36B28575708C46A81DC32F19252D.

[68] Sec. 73, 4th sentence, Sec. 77, 3th sentence, OECD MC Comm. on Art. 1, available on https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#page1.

[69] Sec. 74, 2nd sentence, Sec. 77, 4th sentence, OECD MC Comm. on Art. 1, available on https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#page1.

[70] B.J. Arnold, *Tax Treaties and Tax Avoidance: The 2003 Revisions to the Commentary to the OECD Model*, in *Bullettin – Tax Treaty Monitor*, 2004, p. 250.

[71] Sec. 74, 2nd sentence, Sec. 77, 4th sentence, OECD MC Comm. on Art. 1, available on https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#page1.

[72] G. Kofler, *op. cit.*, p. 106.

Anti-abuse rules included neither in source state's domestic law nor in DTC

In the last scenario, in which an anti-abuse provision is not included either in domestic law nor in DTC, there is no specific provision that can justify a discriminatory treatment in abusive circumstance, so seems that the EU MFN treatment benefit should be granted to the taxpayer. In the author's opinion, this is not the correct conclusion. This issue can be solved by referring to the position recently taken by the ECJ in «Danish cases» (*T Denmark and Y Denmark Aps*[73], *N Luxemburg 1*, *X Denmark A/S*, *C Denmark I* and *Z Denmark APS*[74]), in which the Court stated that is «general principle of EU law that EU law cannot be relied on for abusive or fraudulent ends»[75], so Member State should avoid grant benefit in abusive situation, even though the abusive arrangement is not forbidden by a specific domestic anti-abuse provision because the principle of legal certainty cannot apply to such cases. Since EU MFN treatment constitutes an EU law benefit, this should be denied by Member State in abusive circumstances according to the general EU anti-abuse principle. That means that the general EU anti-abuse principle represents a «justification» of the discriminatory treatment. Also, in this case, we can exclude a conflict between the aforesaid general EU anti-abuse principle and the DTC applicable to the taxpayer claiming the MFN treatment. Since (as we have seen before) domestic SAAR and GAAR can be found in line with DTC and given that the same rules must comply with the general EU anti-abuse principle, the latter also should be considered consistent with the DTC's guiding principle, according which: «the benefits of a double taxation convention should not be available where a main purpose for entering into certain transactions or arrangements was to secure a more favourable tax position and obtaining that more favourable treatment in these circumstances would be contrary to the object and purpose of the relevant provision»[76].

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[73] Court of Justice, Judgment 26 February 2019, Joined Cases C-116/16 and C-117/16, *Skatteministeriet v. T Danmark and Y Denmark Aps*, ECLI:EU:C:2019:135, para. 86, 97, 89 and 90.

[74] Court of Justice, Judgment 26 February 2019, Joined Cases C-115/16, C-118/16, C-119/16 and C-229/16 N Luxemburg 1, *X Denmark A/S, C Denmark I and Z Denmark APS v. Skatteministeriet*, ECLI:EU:C:2019:134.

[75] Court of Justice, Judgment 26 February 2019, Joined Cases C-115/16, C-118/16, C-119/16 and C-229/16 N Luxemburg 1, *X Denmark A/S, C Denmark I and Z Denmark APS v. Skatteministeriet*, ECLI:EU:C:2019:, para. 90.

[76] Sec. 61, 2nd sentence, OECD MC Comm. on Art. 1, available on https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_

In conclusion, EU MFN treatment can be refused in the context of treaty shopping, because in that case, the discriminatory treatment of the source state would be «justified» based on domestic anti-abuse rules or DTC's anti-avoidance provisions or according to the general EU anti-abuse principle. Definitely, in this perspective, the anti-abuse justification would be the «antidote» against the residual treaty shopping loopholes of the EU MFN treatment principle.

2.3.3. Effects on EU and non-EU «investors»

The application of the anti-abuse justification would avoid cases of «abusive» double non-taxation and use «conduit» companies.

In case of a discrimination in breach of the free of movement of capital (art. 63-66 TFEU), the anti-abuse justification would impose to source state to deny the EU MFN treatment to EU and non-EU investors when, as the combined effect of that advantage and the double tax relief granted by the resident state, the taxpayer benefit from a double non-taxation. The source state's denial of the beneficial treatment would be justified not on the simple reason of double non-taxation (because ECJ does not accept it as a justification in itself[77]), but on the circumstance that the latter effect derives from an «abusive» claim of the EU MFN treatment benefit[78]. The same treatment would apply to EU citizen and undertaking when the discrimination involves the freedom of establishment (art. 49-53 TFEU).

When non-EU investors, in the application of the free movement of capital, try to benefit from the EU MFN treatment, through «conduit» companies set-up in a Member States, the (Member State) source state is requested to deny the advantage based on the anti-abuse justification. The

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[77] Court of Justice, Judgment 3 October 2002, Case C-136/00, *Rolf Dieter Danner*, ECLI:EU:C:2002:558; Court of Justice, Judgment 16 July 1998, Case C-264/96, *Imperial Chemical Industries plc (ICI) v Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:1998:370, para. 28; Court of Justice, Judgment 21 September 1999, Case C-307/97, *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt,* ECLI:EU:C:1999:438, para. 50; Court of Justice, Judgment 12 December 2002, Case C-385/00, *F.W.L. de Groot v Staatssecretaris van Financiën*, ECLI:EU:C:2002:750, para. 103.

[78] Court of Justice, Judgment 26 February 2019, Joined Cases C-116/16 and C-117/16, *Skatteministeriet v. T Danmark and Y Denmark Aps*, ECLI:EU:C:2019:135, para. 90 («general principle of EU law that EU law cannot be relied on for abusive or fraudulent ends»).

result is that in the case of treaty shopping investors cannot have access to the MFN treatment.

2.3.4. The proportionality test

The anti-abuse justification would pass the «proportionality test» when the MFN treatment is requested by a «conduit» company (according to the recent ECJ «Danish cases») or results in an «additional» benefit.

More specifically, the last test regards the proportionality of the anti-abuse justification. According to the «proportionality test», the anti-abuse justification of discrimination must be «appropriate» to fight the double non-taxation or treaty shopping arrangement and not go further what is «necessary» to achieve that purposes.

With regards to the freedom of establishment, the ECJ has stated that the « proportionality test» requests that the justified discrimination addresses only the artificial arrangement and not also the genuine structure[7980]. However, in the «Danish cases» ECJ specified that also a «conduit» company can be considered an «artificial» structure, because «the artificiality of an arrangement is capable of being borne out by the fact that the relevant group of companies is structured in such a way that the company which receives the dividends paid by the debtor company must itself pass those dividends on to a third company»[81]. So, discriminatory treatment

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[79] Court of Justice, Judgment 13 December 2005, Case C-446/03, *Marks & Spencer plc v. David Halsey (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:2005:763, para. 4; Court of Justice, Judgment 12 September 2006, Case C-196/04, *Cadbury Schweppes plc e Cadbury Schweppes Overseas Ltd v. Commissioners of Inland Revenue*, ECLI:EU:C:2006:544, para. 51 and 55; Court of Justice, Judgment 14 December 2006, Case C-170/05, *Denkavit Internationaal BV and Denkavit France SARL v Ministre de l'Économie, des Finances et de l'Industrie*, ECLI:EU:C:2006:783, para. 30; Court of Justice, Judgment 13 March 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue*, ECLI:EU:C:2007:161, para. 72 and 74; Court of Justice, Judgment 22 May 2008, Case C-162/07, *Ampliscientifica Srl and Amplifin SpA v Ministero dell'Economia e delle Finanze and Agenzia delle Entrate*, ECLI:EU:C:2008:301, para. 27 and 28; Court of Justice, Judgment 18 June 2009, Case C-303/07, *Proceedings brought by Aberdeen Property Fininvest Alpha Oy*, ECLI:EU:C:2009:377, para. 63.

[80] G. Kofler, *op. cit.*, p. 106.

[81] Court of Justice, Judgment 26 February 2019, Joined Cases C-116/16 and C-117/16, *Skatteministeriet v. T Danmark and Y Denmark Aps*, ECLI:EU:C:2019:135, para. 103; Court of Justice, Judgment 26 February 2019, Joined Cases C-115/16, C-118/16, C-119/16 and C-229/16 N Luxemburg 1, *X Denmark A/S, C Denmark I and Z Denmark APS v. Skatteministeriet*, ECLI:EU:C:2019:134, para. 130.

of «conduit» companies can be justified without fail the «proportionality test». This conclusion remain is also valid for the discriminatory treatment of «conduit» companies in breach of free movement of capital.

On the other side, whenever the application of MFN treatment results in a double non-taxation for EU citizen and undertaking, the anti-abuse justification of the discrimination would pass the «proportionality test». Since the resident country already relieves the taxpayer from the double taxation, the source's state denial of MFN treatment is proportionate insofar the granting of that «additional» advantage would result in a double non-taxation benefit for the taxpayer.

3. Compatibility of EU anti-abuse justification approach with Action 6 BEPS

3.1. Actual discrepancies between EU law and Action 6 BEPS

The position taken by the ECJ in *ACT Group Litigation* case[82], according with a non-resident to whom a LOB («Limitation on Benefits») clause included in a DTC applies is not in comparable situation of a non-resident to whom that such DTC's LOB clause does not apply, can create problem of compatibility between the EU fundamental freedoms and the measures provided by Action 6 of the BEPS Project[83].

Notably, it should be assessed if the LOB and the PPT clauses, conceived by the Action 6 BEPS and included in art. 29 of OECD Model 2017, create problems concerning the EU law rules according which an anti-abuse provision should:

– address only the «wholly artificial arrangements»[84];
– be applied only in a case-by-case analysis[85];

[82] Court of Justice, Judgment 13 March 2007, Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v Commissioners of Inland Revenue*, ECLI:EU:C:2007:161, para. 88 and 91.

[83] F. Debelva - D. Scornos - J. Van den Berghen - P. Van Braband, *op. cit.*, p. 135.

[84] Court of Justice, Judgment 3 October 2002, Case C-136/00, *Rolf Dieter Danner*, ECLI:EU:C:2002:558; Court of Justice, Judgment 16 July 1998, Case C-264/96, *Imperial Chemical Industries plc (ICI) v Kenneth Hall Colmer (Her Majesty's Inspector of Taxes)*, ECLI:EU:C:1998:370, para. 26; Court of Justice, Judgment 12 December 2002, Case C-324/00, *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt,* ECLI:EU:C:2002:749, para. 37.

[85] Court of Justice, Judgment 18 September 2003, Case C-346/00, *United Kingdom of Great Britain and Northern Ireland v Commission of the European Communities*, ECLI:EU:C:2003:474,

– give the taxpayer the right to provide evidence about commercial justification underlying the operation if there is a presumption abuse[8687].

In relation to the compatibility of the LOB clause with EU law, it could be found that LOB rules also address not «wholly artificial arrangement»[88].

Regarding the PPT clause (Principle Purpose Test, included in art. 29.9 of OECD Model 2017[89]), although it does not discriminate residents of the states that have not implemented that provision and residents of the states that have done that, some problems are created by the broad interpretation of such clause as suggested by Action 6 BEPS[9091].

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para. 43; Court of Justice, Judgment 12 December 2002, Case C-324/00, *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt,* ECLI:EU:C:2002:749, para. 38.

[86] Court of Justice, Judgment 5 May 2011, Case C-267/09, *European Commission v Portuguese Republic*, ECLI:EU:C:2011:273, para. 42; Court of Justice, Judgment 18 September 2003, Case C-346/00, *United Kingdom of Great Britain and Northern Ireland v Commission of the European Communities*, ECLI:EU:C:2003:474, para. 43; Court of Justice, Judgment 12 December 2002, Case C-324/00, *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt,* ECLI:EU:C:2002:749, para. 38.

[87] F. Debelva - D. Scornos - J. Van den Berghen - P. Van Braband, *op. cit.*, pp. 139-141.

[88] Particularly, by applying the lob rules: the «stock-exchange test», beyond the «wholly artificial arrangements», also address the «genuine» economic activities, because a company can have a «real» economic interest to be listed in another country; the «ownership test» would be failed by a company having foreign shareholders, because of the absence of case-by-case analysis on the «genuine» nature of the operation, although it is not set-up for treaty shopping purposes; the «base erosion test» only take care of the formal characterization of operations, without investigate about its real scope; the «business test» penalize genuine activities when the income received is not connected with or incidental to the business performed in the state of residence (e.g «portfolio investment»), although in the absence of tax abusive purposes; the «derivative benefits test» more probably address, for example, genuine undertaking whose shareholders are resident in third countries having a DTC with the source country that provides a withholding tax higher than the «0» rate ones included in the DTC containing the LOB clause; according to the «discretionary relief clause» , competent authority can deny the treaty benefits when «one» of the principal purpose of the operator is to obtain treaty benefits , also when the undertaking is genuine (not «wholly artificial arrangement») because, as stated by ECJ, has not the «sole» purpose to get treaty benefits.

[89] OECD MC art. 29.3 («Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention») available on https://read.oecd-ilibrary.org/taxation/model-tax-convention-on-income-and-on-capital-condensed-version-2017_mtc_cond-2017-en#page1.

[90] K.N. Pedersen - S. Schults*, op. cit.*, p. 332.

[91] Even though many «substantial» elements should be taken in account to assess the cases

The problem remains when a PPT clause is used in combination with the LOB clause because taxpayers who fail the LOB test in art. 29, sec. 1 to 6, are not subject to the PPT, with the same effect of the simple LOB application. Then the LOB clause can result in breach with EU law and the PPT test is not always capable of offsetting this effect[92].

3.2. Compatibility of the EU MFN treatment with the Action 6 BEPS

3.2.1. The anti-abuse justification in line with the Action 6 BEPS

The application of the LOB clause (alone or in combination with the PPT clause) in some case can be founded incompatible with EU fundamental freedoms unless MFN treatment applies.

In particular, the simple application of MFN treatment does not make a difference between «genuine» activities and «wholly artificial arrangements» at the level of «comparability test», with the effect that non-residents in a comparable factual and legal situation («horizontal comparison») should receive the same treatment. In a situation in which a LOB clause applies, alone or combined with a PPT clause, treaty benefits can be denied at level of «justification test». However, only when benefits are denied to a «genuine» undertaking, the DTC anti-abuse clause would not apply, as required by the application of EU freedom of establishment.

Although in this case seems that DTC anti-abuse rules can collide with EU fundamental freedoms, the conflict is only «apparent». A Member State can disapply a DTC anti-abuse rules by granting DTC benefits to a «genuine» undertaking in tax treaty «abusive» (although not EU «abusive») circumstances in the «exercise» of its taxing right. Since the tax treaty's anti-abuse rules protect states in the exercise of their taxing right, the fact that a Member State «unilaterally» disapplies such anti-abuse rules should be considered not different from a «unilateral extension» of domestic benefits that do not affect the right of the other contracting state[93]. After all, by giving

of treaty abuse according to the PPT clause, states can implement that provision in a way to require an administrative process of approval or an advisory committee to use the PPT. That can result in a different implementation of the anti-abuse provision by the Member States that could not match with the general EU anti-abuse principle and then founded in breach of fundamental freedoms.

92 K.N. Pedersen - S. Schults, *op. cit.*, p. 332.

93 The state that disapplies the DTC's anti-abuse rules still comply with the «restriction» (and the «allocation») of its taxing rights agreed through DTC; in fact, its taxing rights would result

additional benefits (which means taxing less) source state still comply with the «restriction» (*rectius* «allocation») of its taxing right agreed in DTC. That «unilateral extension» of domestic benefit would not break the DTC's obligations, (also in this case) as ECJ stated in *Saint-Gobain*[94]. In conclusion, the application of an EU MFN treatment principle would make EU law compatible with the Action 6 BEPS' measures.

3.2.2. EU MFN treatment: a step forward

In the author's opinion, the application of the EU MFN treatment principle would protect the Internal Market neutrality from treaty shopping in a more «consistent» way than the «absolute» Action 6 BEPS' anti-abuse based approach.

In fact, even in presence of the MLI (art. 7 of the «Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS» about «Prevention of Treaty Abuse»[95]), from a source state prospective, the implementation of different options of LOB and PPT clauses inside DTC would result in diversified effects («mismatching effect») of their application depends on the state of residence of investors. The different treatment of non-resident investors is inconsistent with the Internal Market neutrality because it results in the breach of the above proposed «substantial» EU principle of equality. Moreover, from a more practical perspective, anti-abuse rules only apply when all the countries agree about those and their different application can create several loopholes.

Differently, from a source state prospective, the application of different DTC's LOB and PPT clauses options in presence of the EU MFN treatment principle would result in a more «homogeneous» treatment of non-resident investors, because those clauses would be disapplied in the

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even more restricted as the effect of the unilateral granting of that benefit.

[94] Court of Justice, Judgment 21 September 1999, Case C-307/97, *Compagnie de Saint-Gobain, Zweigniederlassung Deutschland v Finanzamt Aachen-Innenstadt,* ECLI:EU:C:1999:438, para. 57 and 59 («57. […]since such an extension would not in any way affect the rights of the non-member countries which are parties to the treaties and would not impose any new obligation on them» with the effect that «59. As far as the exercise of the power of taxation so allocated is concerned, the Member States nevertheless may not disregard Community rules. According to the settled case-law of the Court, although direct taxation is a matter for the Member States, they must nevertheless exercise their taxation powers consistently with Community law»).

[95] OECD MLI Art. 7, *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS*, Paris, OECD, 2018, available at https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-BEPS.pdf.

presence of «genuine» undertakings to preserve the freedom of establishment and, at the same time, the Internal Market neutrality.

4. Conclusions

The ECJ rejected the MFN treatment principle in EU law without providing serious logical and legal motivation, opening the gateway to Member State to tax treaty «competition» that treat to undermine the neutrality of the Internal Market. Moreover, in the absence of an MFN treatment principle, EU law results not compatible with the Action 6 BEPS' anti-abuse clauses (LOB and PPT) because these rules also address «non-artificial» arrangements that are protected by the EU fundamental freedoms. The ECJ's hidden assumption seems that Member State freedom to grant different treatment to non-resident investors according to their residence is more important than the neutrality of the Internal Market.

In the author's view, to achieve the neutrality of the Internal Market, EU law needs a «substantial» principle of equality according to which «horizontal discrimination» and «vertical discrimination» should receive the same disapproval also when tax treaty benefits are involved. Even if a source state «allocate» its taxing rights through tax treaties, only the «exercise» of such taxing rights is capable discriminating foreign investors according to their residence State. While the «allocation» of taxing right produces effects between states («balancing» their fiscal power), only the «exercise» taxing power affects the position of taxpayers, resulting in higher or lower tax burden. This tax burden, as an additional economic cost, can trigger «inequality» between taxpayers, resulting in discriminatory treatment in breach of the fundamental freedoms. Furthermore, also the EU arm's length principle found out by the ECJ in the field of «state aid» implies the existence of a «substantial» EU principle of equality.

According to the proposed «substantial» EU principle of equality, in the context of the «discrimination analysis» non-residents in similar factual and legal circumstances should receive equal treatment as the effect of the «comparability test». In the author's opinion, the «comparability test» should consider only the source state's perspective and not even the eventually resident state's «neutralization» of the source state's discriminatory measure (through double tax relief). Since the «comparability test» is the logical premise of the «discrimination analysis», there is no reason to

wonder in advance if a discriminatory treatment can be neutralized for the «comparability test». Furthermore, considering that in this case the object of the «discrimination analysis» is the source state's exercise of taxing right, there is no reason to consider in the «comparability test» elements only «imputable» to the resident state. Besides the «comparability test» should take into consideration only the taxpayer's «personal» situation subjected to the «discrimination analysis», without taking into account other taxpayers' «personal position» (connected or not connected to the taxpayer).

The implementation of the MFN treatment principle into EU Internal Market will have the advantage to stop treaty shopping inside EU laid by Member States' residents because those would have no reason to set-up an «intermediary» or «conduit» company in a different Member State since source state treatment of inbound investment would be the same. However, the author discovers that the «simple» application of such MFN treatment principle would allow some (EU and non-EU) investors to benefit from a better combined source-resident states' tax treatment compared to the one applicable to other investors, as the effect of the different double tax relief rules applied by resident countries. Another problem would remain in the term of treaty shopping, putting in place by non-EU residents using EU resident «conduit» entities to take advantage of the EU MFN treatment. These problems cannot be solved at the level of «comparability test».

Nevertheless, the «horizontal discriminatory» treatment can be still justified by reasons of public interest according to the «justification test». In the author's opinion, elements that must be excluded from the «comparability test», because considered unrelated to the factual and legal condition of the taxpayer, can find their «natural» place into the «justification test» to assess if «discriminatory measure» can be «saved» by reasons of «public interest». The anti-abuse justification would be the «antidote» against the residual treaty shopping loopholes of the EU MFN treatment principle.

An in-deep reading of the recent ECJ «Danish cases» allow reopening the discussion about the recognition of an MFN treatment principle in EU law. MFN treatment can be refused in the context of treaty shopping because the discriminatory treatment of the «conduit» companies would be «justified» based on domestic anti-abuse rules or DTC's anti-avoidance provisions or according to the general EU anti-abuse principle stated by ECJ in the «Danish cases». The same conclusion remains valid for the cases of double non-taxation resulting from the «abusive» claim of the EU MFN treatment benefit. Moreover, in the case of «abusive» double non-taxation

or use «conduit» companies, the anti-abuse justification would pass the «proportionality test». Making it more simple, while currently, by denying the application of the EU MFN treatment ECJ catches the «bad» fish by poisoning all the water in the aquarium (where «good» fish also swim), the author proposes to catch only the «bad» fish by using appropriate baits.

The position taken by the ECJ in *ACT Group Litigation* case, according with a non-resident to whom a LOB clause included in a DTC applies is not in comparable situation of a non-resident to whom that such DTC's LOB clause does not apply, can raise problems of compatibility between the EU fundamental freedoms and the measures provided by Action 6 of the BEPS Project when «genuine» activities are involved. In the author's opinion, the application of the LOB clause (alone or in combination with the PPT clause) in some cases can be founded incompatible with EU fundamental freedoms unless MFN treatment applies. Since MFN treatment does not differentiate between «genuine» activities and «wholly artificial arrangements» at the level of «comparability test», non-residents in a comparable factual and legal situation («horizontal comparison») should receive the same treatment. In a situation in which a LOB clause applies, alone or combined with a PPT clause, treaty benefits can be denied at level of «justification test». However, only when benefits are denied to a «genuine» undertaking, DTC anti-abuse clause would not apply, as required by the application of EU freedom of establishment. Although in this case seems that DTC anti-abuse rules can collide with EU fundamental freedoms, the conflict is only «apparent». A Member State can disapply a DTC anti-abuse rules by granting DTC benefits to a «genuine» undertaking in tax treaty «abusive» (although not EU «abusive») circumstances in the «exercise» of its taxing right.

In conclusion, beyond preserving the neutrality of the Internal Market, the recognition of an EU MFN treatment principle would reconcile the actual clash between EU law and Action 6 BEPS' anti-abuse rules (LOB and PPT clauses).