AB v Finanzamt Köln-Süd (C-627/22)

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1. Background

The case *AB v Finanzamt Köln-Süd,* which was decided by the CJEU in May 2024,[1] concerns the guarantees under the EU-Swiss Agreement on the Free Movement of Persons (AFMP)[2] as it pertains to the taxation of cross-border employees. The AFMP was concluded between the European Communities and its Member States on the one hand and the Swiss Confederation on the other, and forms part of the Union legal order (Arts. 216 and 217 TFEU). It is binding upon the institutions of the EU and its Member States (Art. 216 para. 2 TFEU).[3]

Employees working in Germany are subject to German wage tax which is levied as a withholding tax. German resident employees may opt for voluntary tax assessment.[4] If they choose to do so, income-related expenses can be deducted, and the wage tax previously paid is credited to the final tax liability. Following the CJEU's judgement in *Schumacker,*[5] cross-border commuters can – under certain conditions – also choose to file a tax assessment. They can then deduct income-related expenses, and in particular profit from joint tax assessment with a non-

1 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431. On this case see e.g. the case note by S. Piotrowski, EuGH v. 30.05.2024 – C-627/22, Abkommen zwischen der Europäischen Gemeinschaft und der Schweizerischen Eidgenossenschaft über die Freizügigkeit – Arbeitnehmer eines Mitgliedstaats, der seinen Wohnsitz in die Schweiz verlegt hat, Internationale Steuerrundschau 2024, p. 278. For comments on the Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, see R. Ismer/S. Piotrowski/S. Güllich in G. Kofler et al. (eds.), *CJEU Recent Developments in Direct Taxation 2023* (Vienna: Linde, 2024) 1, 5 et seqq.

2 Agreement of 21 June 1999 between the European Community and its Member States, of the one part, and the Swiss Confederation, of the other, on the free movement of persons – Final Act – Joint Declarations, which entered into force on 01 June 2002, ABl. 2002, L 114, p. 6.

3 See on the AFMP e.g. R. Ismer, in: C. Hermann et. al. para. (eds.), *Einkommensteuer- und Körperschaftsteuergesetz* (Köln: Otto Schmidt Verlag, 2020) Einführung zum EStG, m.n. 566 et seqq.; K. Spies, *Die Wirkung des Freizügigkeitabkommens EU/Schweiz im Steuerrecht*, StuW 2017, p. 48 et seqq.

4 Under Sec. 46 para 2 no. 8 of the EStG.

5 CJEU, 14 February 1995, C-279/93, *Finanzamt Köln-Altstadt v Schumacker*, ECLI:EU:C:1995:31, para. 49.

resident spouse. In its 2013 judgement in *Ettwein,* the CJEU decided that this privilege had to be extended to cross-border Swiss cases.[6]

In all other cases, non-resident taxpayers deriving employment income in Germany are subject to limited tax liability. The wage tax is then, in principle, final. However, EU/EEA nationals residing in an EU/EEA State may apply for tax assessment,[7] which at least allows them to deduct income-related expenses. The question at issue in this case is whether this voluntary assessment must also be possible for Swiss residents deriving employment income in Germany.

2. Facts of the Case and Referral Question

The German national AB, a manager of a German company, had lived in Switzerland since 2016.[8] From 2017 to 2019, he derived employment income from his German employer. While living in Switzerland, AB either travelled to Germany by car or worked remotely from home in Switzerland. AB was subject to limited tax liability in Germany. His employer withheld wage tax and remitted it to the German tax authorities. AB incurred income-related expenses as he used a private car purchased under a leasing contract for business travel to Germany. He also owned two immovable properties located in Germany from which he derived rental income.

AB filed an income tax return declaring both income from the immovable properties and employment income. As to the latter, AB sought the benefit of Sec. 50 para 2 sent. 2 no. 4 lit. b EStG which allows for a voluntary tax assessment. The provision allows employees to receive a tax refund as the German wage tax does not take into account income-related expenses. However, since this provision only applies to EU/EEA nationals residing in another EU or EEA State,[9] the notice of assessment issued by the tax authorities did not include AB's employment income (and hence the related expenses). AB lodged an administrative appeal and ultimately took legal action before the Finanzgericht *Köln* (Financial Court of Cologne).

The *Finanzgericht Köln* referred a question on the interpretation of the AFMP to the CJEU. It asked whether the denial of a voluntary tax assessment infringes upon Arts. 7 and 15 AFMP in conjunction with Art. 9 para 2 of annex 2 to the AFMP. In this, the Court referred to two potentially relevant comparators, namely first German or EU/EEA nationals residing in Germany and second Ger-

6 CJEU, 28 February 2013, C-425/11, *Ettwein*, ECLI:EU:C:2013:121. See on this judgement e.g. A. Cloer, *Ausdehnung der Schumacker-Rechtsprechung auch auf Schweizer Grenzgänger*, DB 2013, p. 1141 et seqq.

7 See Sec. 50 para 2 sent. 1 and 2 sent. 2 no. 4 EStG.

8 See Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, paras. 20 et seqq.

9 Sec. 50 para. 2 sent. 7 EStG.

man or EU/EEA nationals residing in an EU/EEA Member State other than Germany. Both comparators can voluntarily opt for a tax assessment under national law and thus deduct income-related expenses, ultimately resulting in a tax refund.

3. Opinion of AG Campos Sánchez-Bordona as of 16 November 2023

The Advocate General (AG) had opined that the denial of a voluntary tax assessment infringed upon Arts. 7 and 15 AFMP in conjunction with Art. 9 para 2 of annex 2 to the AFMP.[10] He argued that the AFMP also extends to differences in treatment arising from the place of residence of employed persons covered by the AFMP, even when they are not typical frontier workers.[11] He then explained that the term 'tax concession' within the meaning of Art. 9 para. 2 of Annex I to the AFMP encompasses options available under national law for calculating tax liability in a more favourable way, such as voluntary assessment.[12] While Art. 21 para. 2 AFMP allows residence-based distinctions between taxpayers that are not comparable, he considered that such comparability exists because Germany has allowed EU/EEA nationals residing outside of Germany – and that are therefore subject to limited tax liability – to file for voluntary assessment.[13] The AG then elaborated that the differential treatment could not be justified by the need to ensure the imposition, payment and effective recovery of income tax in Germany, and the objective to forestall tax evasion.[14] Finally, the AG rejected the claim by the German government that the standstill clause of Art. 13 of the AFMP, under which the Contracting Parties undertake not to adopt any further restrictive measures vis-à-vis each other's nationals, could be read as allowing for old restrictions (that existed at the time of the conclusion of the AFMP) to continue to exist.[15]

4. Judgement by the CJEU as of 30 May 2024

The Court followed the Advocate General's opinion and decided that the denial of a voluntary tax assessment infringed upon Arts. 7 and 15 AFMP in conjunction

10 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, para. 68 et seqq. On this see R. Ismer/ S. Piotrowski/ S. Güllich in G. Kofler et al. (eds.), *CJEU Recent Developments in Direct Taxation 2023* (Vienna: Linde, 2024) 1, 5 et seqq.

11 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, para. 68 et seqq.

12 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, para. 71.

13 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, paras. 78–80.

14 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, paras. 87–89.

15 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, paras. 95–99.

with Art. 9 para 2 of Annex 1 to the AFMP. It first explains that AB falls within the category of persons referred to in Articles 1 and 2 of the AFMP.[16] For that purpose, it refers to its case law, according to which Article 2 of the AFMP prohibits any discrimination on grounds of nationality, including against nationals of one Contracting Party who are lawfully resident in the territory of another Contracting Party.

AB also falls within the material scope of Annex I to the AFMP.[17] Even if AB were not an employed frontier worker in the sense of Article 7 of Annex I, the non-discrimination clause of Article 9 para. 2 of Annex I would still apply, as it does not distinguish between employed persons and employed frontier workers.

Given that the right to opt for voluntary assessment makes it possible to claim the deduction of occupational expenses incurred in obtaining income from employment and that any excessive tax withheld in the withholding tax procedure may be refunded, such right constitutes a tax concession.[18] The fact that the right is not available to Swiss residents marks a difference in treatment, as the AFMP also applies to all covert forms of discrimination which, by the application of other distinguishing criteria, such as the criterion of residence, in fact lead to the same result.[19] Article 21(2) AFMP then requires comparability. Generally, residents and non-residents are not in a comparable situation. Yet, the court nevertheless arrives at comparability through a two-pronged argument. First, it points to the possibility that residents of other EU Member States or of a State party to the EEA Agreement may request a voluntary assessment. It concludes that the German legislation accepts comparability between non-residents and residents.[20] Second, the court rejects the arguments brought forward by the German government pertaining to the lack of comparability.[21] The possibility to record professional expenses in the withholding tax procedure is not a fully-fledged alternative. This is because it operates under shorter time limits and requires predictions. which, in case they turn out to be wrong, require, under threat of criminal sanctions, additional action by the taxpayer. Moreover, the voluntary assessment at issue here does not concern personal circumstances. And finally, any arguments regarding impediments to collecting taxes abroad fail to convince as the taxes have already been withheld.

The discrimination cannot be justified under Article 21(3) of the AFMP.[22] As observed above, the voluntary assessment concerns taxes that have already been

16 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 52 et seqq.
17 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 58 et seqq.
18 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 79 et seqq.
19 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 82 et seqq.
20 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 93 et seq.
21 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 95 et seqq.
22 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 103 et seqq.

paid and thus do not need to be recovered. Nor does a justification by the overriding reason in the general interest relating to the need to preserve fiscal coherence apply.[23]

Finally, the court held that the discrimination is not permissible under Article 13 of the AFMP.[24] Under that provision, the Contracting Parties undertake not to adopt any further restrictive measures vis-à-vis each other's nationals in fields covered by that agreement. Despite its heading (standstill clause), the provision does not contain a standstill clause that would be comparable to the substantially different Article 64 TFEU. This is because the wording of the provision apart from its heading does not point to such a result. Neither would such a far-reaching consequence be in accordance with the purpose of the AFMP.

5. Comments

As stated previously, the AB v Finanzamt Köln-Süd case is yet another small piece of the puzzle that is the CJEU's case law on the AFMP in the area of taxation. Nevertheless, the case provides food for thought regarding the correct approach to interpreting the AFMP,[25] in particular regarding the right comparator and comparability, which have to be seen in light of the limit of Art. 16 para. 2 AFMP.

The AG in his opinion had repeatedly mentioned that the discriminatory tax treatment would have to be verified *"by comparison with that afforded to employed persons who, while pursuant an activity similar to that of AB, live in Germany or in other Member States of the European Union or the EEA"*.[26] In a later passage, in discussing comparability under Art. 21 para. 2 AFMP, he had explicitly limited the analysis to the horizontal comparator, i.e. residents of EU/EEA States that are nationals of one of these States.[27] However, in *Wächtler,* the CJEU had already clarified that only the former comparator is valid under the AFMP.[28]

The CJEU departs from the AG's reasoning, as it seems to choose a vertical comparator and establishes comparability between the resident and non-resident situations. Yet in doing so, it takes an interesting path: it establishes comparability based on German legislation which treats particular cases of non-residents (EU/EEA cases) and residents alike. The German resident and the Swiss resident are in a compara-

23 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 107 et seqq.
24 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 110 et seqq.
25 See also R. Ismer/ S. Piotrowski/ S. Güllich in G. Kofler et al. (eds.), *CJEU Recent Developments in Direct Taxation 2023* (Vienna: Linde, 2024) 1, 10 et seqq.
26 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, para. 72, see also paras. 74 et seq.
27 Opinion of Advocate General Campos Sánchez-Bordona, 16 November 2023, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2023:882, para. 78.
28 CJEU, 26 February 2019, C-581/17, *Wächtler,* ECLI:EU:C:2019:138, para. 56. By contrast, blurry in this respect: CJEU, 21 September 2016, C-478/15, *Radgen,* ECLI:EU:C:2016:706, para. 42.

ble situation because the German legislator has decided to treat German residents and EU/EEA residents alike. One may doubt, however, that this truly was the German legislator's decision. The German rule was amended following the CJEU's decision in *Gerritse* as the previous rule did not fully comply with the requirements under EU law.[29] Can there really be voluntary comparability under duress? Or, inverting the perspective: If the Swiss legislator is not under an obligation to grant equal treatment between residents and non-residents from legal sources outside the AFMP, does this imply that it would not have to treat residents and non-residents alike under the AFMP? If taken seriously, this would result in a rather interesting asymmetry, which would not be in line with the public international law principle of reciprocity.

The court's travails seem to go back to Article 16(2) AFMP, according to which only the CJEU's case law prior to the date of signature of the AFMP shall be taken into account for the interpretation of the AFMP. This rule apparently led the Advocate General to base his reasoning on the *Schumacker* decision. Commendably, the court avoids this pitfall. As indicated, the facts of the case at hand correspond to the *Gerritse* case rather than the *Schumacker* case. Admittedly, the *Gerritse* case was decided after the signature of the AFMP and is thus not directly relevant for the interpretation of the AFMP. A reference to the *Gerritse* case thus seems to be ruled out by Article 16(2) AFMP. Yet, the core of that ruling can already be found in the *Asscher* case.[30] While in contrast to the Advocate General, the court does refer to that ruling,[31] it should have been clearer regarding the significance of the *Asscher* decision for the present case. In future, the CJEU should be more transparent on the limit of Article 16 (2) AFMP and carefully explain the transferability. In the eyes of the court, this may admittedly amount to a *probatio diaboli,* given that the CJEU considers that it discovers the law rather than makes it. Nevertheless, the distinction underlies Article 16(2) of the AFMP and should be taken seriously.

29 See E. Reimer, in: P. Brandis/B. Heuermann (eds.), *Ertragsteuerrecht,* (Munich, Vahlen: 2024), § 50 EStG, para 103.

30 CJEU, 27 June 1996, C-107/94, *Asscher*, ECLI:EU:C:1996:251, para. 47.

31 CJEU, 30 May 2024, C-627/22, *AB v Finanzamt Köln-Süd*, ECLI:EU:C:2024:431, paras. 86 et seq.

Germany: Familienstiftung C-142/24

Alexander Rust

1. Facts and legal Background of the Case[1]

The German Inheritance and Gift Tax Act distinguishes between different tax classes, depending on the family relationship between the donor/deceased and the donee/heir. The tax classes are relevant for the amount of the tax allowance and the tax rate. The tax-free amount varies between EUR 20,000 in class III and EUR 500,000 for certain taxpayers of class I.[2] The tax rates vary between 7% and 50%, depending on the amount of the donation and the tax class of the taxpayer.[3] The transfer of money to a foundation is also subject to inheritance and gift tax.[4] For transfers of money to foundations resident in Germany, the tax-free amount and the tax rate depend on the family relationship between the founder and the beneficiary who has the most distant family relationship.[5] Transfers of money to foundations resident outside of Germany are always subject to tax class III. As a result, the lowest possible tax-free amount and the highest tax rate applies. Family foundations resident in Germany are subject to a substitute inheritance tax.[6] Every 30 years, their property is treated as being transferred from parents to children. Non-resident foundations are not subject to such substitute inheritance tax.

A resident of Germany created a family foundation in Liechtenstein and transferred a significant amount of money to the foundation. Under its articles of association, the purpose of the foundation was to sponsor and support the children of

1 Preliminary ruling by Finanzgericht Cologne, 30 November 2023, 7 K 217/21, IStR 2024, 317. See the remarks by K. Dorn, DStRK 2024, 97; P. Lennert/A. Löhmer, IStR 2024, 648; M. Morawitz, DStRE 2024, 540; A. Eiling/A. Keßeler, IWB 2024, 305; M. Gräfe/M. Weber, ZEV 2024, 562; Oellerich, Erbschaft- und Schenkungsteuerrecht, in H. Schaumburg/J. Englisch/L. Dobratz, Europäisches Steuerrecht, 3rd ed. 2025, m. no. 10.75a.

2 See Sec. 16(1) German Inheritance and Gift Tax Act.

3 See Sec. 19(1) German Inheritance and Gift Tax Act.

4 See Sec. 1(1) N° 2 in connection with Sec. 7(1) N°8 German Inheritance and Gift Tax Act.

5 See Sec. 15(2) German Inheritance and Gift Tax Act.

6 See Sec. 1(1) N°4 German Inheritance and Gift Tax Act.

the founder. The beneficiaries of the foundation were the founder, the founder's children and their children. The founder filed a tax return for gift tax purposes and argued that she should be entitled to the higher tax-free allowance and the lower tax rate for transfers of money to German foundations as denying these benefits to transfers of money to a Liechtenstein foundation violated Art. 40 of the EEA-Agreement.[7] The German tax administration applied the lower tax-free allowance and the higher tax rate in conformity with the provisions of the German Inheritance and Gift Tax Act for transfers of money to foreign foundation. The German tax administration could not see a violation of the free movement of capital. According to the German tax administration, the less favourable treatment was justified by the need to preserve the cohesion of the German tax system, as foreign foundations were not subject to a substitute inheritance tax. The foundation filed an appeal against the tax assessment and the *Finanzgericht Cologne* – the tax court of first instance – decided to stay the proceedings and refer the following questions to the CJEU for a preliminary ruling:

> Must Article 40 of the Agreement on the European Economic Area (EEA Agreement) of 2 May 1992 be interpreted as precluding a Member State's national legislation on the levying of inheritance and gift tax which applies the highest tax class (III) for the taxation of an inter vivos transfer of assets to a foundation established abroad even where the foundation is established essentially in the interests of a family or certain families (family foundation), whereas for a family foundation established on national territory in an equivalent situation, the tax class depends on the relationship between the most distantly related beneficial owner under the foundation's articles of association and the donor (founder), which results, for family foundations established on national territory, in the application of the more favourable tax classes I or II.

2. Legal Reasoning

2.1. Applicable Freedom

Transfers of money to a Liechtenstein foundation are protected by the free movement of capital enshrined in Article 40 EEA-Agreement.

2.2. Restriction

Providing an endowment fund to a Liechtenstein family foundation is subject to a lower tax-free allowance and to a higher tax rate compared to providing the same endowment fund to a German family foundation. Both situations are comparable.

7 Art. 40 EEA-Agreement has the following wording: "Within the framework of the provisions of this Agreement, there shall be no restrictions between the Contracting Parties on the movement of capital belonging to persons resident in EC Member States or EFTA States and no discrimination based on the nationality or on the place of residence of the parties or on the place where such capital is invested …"

2.3. Justification

A more burdensome treatment of the cross-border movement can be justified by overriding reasons in the general interest. The measure must pursue a legitimate purpose, must not go beyond what is necessary to achieve that goal and must be proportionate. The Court of Justice has recognized that the need to preserve the cohesion of the tax system may justify a more burdensome treatment.[8] A tax system can be regarded as coherent if there exists a close link between the tax advantage and the tax disadvantage. The German tax administration argued that this close link exists between the higher tax-free allowance and the lower tax rate for transfers to German foundations on the one hand and the additional tax burden in the form of a substitute inheritance tax every 30 years for German foundations on the other hand. Different tax rates and allowances for transfers to German and foreign family foundations have existed since 1959, while the substitute inheritance tax for German family foundations was only introduced in 1974. Although the link between tax advantage and tax disadvantage has not existed from the outset, the German legislator justified the better tax treatment of German foundations when receiving an endowment with the existence of a substitute inheritance tax.[9]

However, a tax measure can only be justified by the need to preserve the cohesion of the tax system if the link between the tax disadvantage and the tax advantage is sufficiently close.[10] Here, the amounts saved through the more beneficial tax rate and the higher tax allowance for German foundations are completely unrelated to the additional tax burden due to the substitute inheritance tax. Tax advantage and tax disadvantage do not even coincide in all cases. A German foundation may benefit from the lower tax rate and the higher tax-free allowance without being subject to the substitute inheritance tax. A substitute inheritance tax is only due after 30 years and not all family foundations will last for 30 years. As a result, the tax disadvantage for foreign foundations cannot be justified by cohesion and, therefore, violates the free movement of capital enshrined in Art. 40 EEA-Agreement.

3. Consequences

The Court of Justice will likely decide in favour of the Liechtenstein family foundation. This means that the endowment will benefit from the lower tax rates and the higher tax-free allowance. The judgement will be based on Article 40 EEA-

8 See ECJ of 28 January1992, C-204/90 (Bachmann), ECR 1992, I-249; ECJ of 28 January 1992, C-300/90 (Commission v Belgium), ECR 1992, I-305.

9 BT-Drs. 7/1333 p. 5.

10 See ECJ of 28 January1992, C-204/90 (Bachmann), ECR 1992, I-249; ECJ of 11 August 1995, C-80/94 (Wielockx), ECR1995, I-2493; ECJ of 14 November 1995, C-484/93 (Svensson/Gustavsson), ECR 1995, I-3955; ECJ of 6. June 2000, C-35/98 (Verkooijen), ECR 2000, I-4071; ECJ of 8 March 2001, C-397/98 and C-410/98 (Metallgesellschaft / Höchst), ECR 2001, I-1727; see also A. Rust, Die Hinzurechnungsbesteuerung (2006), p. 144 et seq.

Agreement but will have consequences for all foreign family foundations as Article 63 TFEU, which applies to all cross-border capital movements, is worded in a similar way to Article 40 EEA-Agreement. Although the disadvantages for transfers of money to foreign family foundations already existed before the end of 1993, the standstill clause of Article 64 TFEU cannot save the provisions of the German Inheritance and Gift Tax Act, as transfers of money to family foundations do not qualify as direct investments.[11]

11 See the annex to the directive 88/361/EEC N° I and XI lit. b; see also P. Lennert/A. Löhmer, IStR 2024, 648 (653).