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Case C-253/03

CLT-UFA SA

v

Finanzamt Köln-West

(Reference for a preliminary ruling from the Bundesfinanzhof)

(Freedom of establishment – Tax legislation – Tax on company profits)

Summary of the Judgment

Freedom of movement for persons – Freedom of establishment – Tax legislation

(EC Treaty, Art. 52 (now, after amendment, Art. 43 EC) and Art. 58 (now Art. 48 EC))

Article 52 of the Treaty (now, after amendment, Article 43 EC) and Article 58 of the Treaty (now Article 48 EC) preclude a national law which, in the case of a branch of a company having its seat in another Member State, lays down a tax rate on the profits of that branch which is higher than that on the profits of a subsidiary of such a company where that subsidiary distributes its profits in full to its parent company.

The second sentence of the first paragraph of Article 52 of the Treaty expressly leaves traders free to choose the appropriate legal form in which to pursue their activities in another Member State and that freedom of choice must not be limited by discriminatory tax provisions. The freedom to choose the appropriate legal form in which to pursue activities in another Member State thus primarily serves to allow companies having their seat in a Member State to open a branch in another Member State in order to pursue their activities under the same conditions as those which apply to subsidiaries. The refusal to apply the reduced tax rate to branches renders the possibility, for companies having their seat in another Member State, of exercising the right to freedom of establishment through a branch less attractive and thus restricts the freedom to choose the appropriate legal form in which to pursue activities in another Member State.

It is for the national court to determine the tax rate which must be applied to the profits made by a branch by reference to the overall tax rate which would have been applicable if the profits of a subsidiary had been distributed to its parent company.

(see paras 14-15, 17, 31, 37, operative part 1-2)

JUDGMENT OF THE COURT (Third Chamber)

23 February 2006 (*)

(Freedom of establishment – Tax legislation – Tax on company profits)

In Case C-253/03,

REFERENCE for a preliminary ruling under Article 234 EC from the Bundesfinanzhof (Germany), made by decision of 1 April 2003, received at the Court on 13 June 2003, in the proceedings

CLT-UFA SA

v

Finanzamt Köln-West,

THE COURT (Third Chamber)

composed of A. Rosas, President of the Chamber, J. Malenovský, J.-P. Puissechet, S. von Bahr (Rapporteur) and U. Lõhmus, Judges,

Advocate General: P. Léger,

Registrar: M. F. Contet, Principal Administrator,

having regard to the written procedure and further to the hearing on 29 September 2004,

after considering the observations submitted on behalf of:

- CLT-UFA SA, by A. Raupach and D. Pohl, Rechtsanwälte,
- Finanzamt Köln-West, by K.-H. Vanyek and G. Sasonow, acting as Agents,
- the German Government, by C.-D. Quassowski, M. Lumma and W.-D. Plessing, acting as Agents,
- the Commission of the European Communities, by R. Lyal and G. Braun, acting as Agents,

after hearing the Opinion of the Advocate General at the sitting on 14 April 2005,

gives the following

Judgment

1 The reference for a preliminary ruling concerns the interpretation of Article 52 of the EC Treaty (now, after amendment, Article 43 EC) and Article 58 of the EC Treaty (now Article 48 EC).

2 That reference was made in the context of a dispute between CLT-UFA SA ('CLT-UFA') and Finanzamt Köln-West (Tax Services Department; 'the Finanzamt') about taxation of the profits of the German branch of CLT-UFA.

The main proceedings and legal background

3 The company CLT-UFA has its seat and central administration in Luxembourg. In 1994 ('the financial year in dispute') it held a branch in Germany.

4 The Finanzamt fixed the taxable amount for corporation tax in respect of CLT-UFA, a company which was subject to limited taxation in Germany on income generated by its German branch during the financial year in dispute, in accordance with Article 5(1) of the Convention between the Grand Duchy of Luxembourg and the Federal Republic of Germany for the avoidance

of double taxation and relating to mutual administrative assistance in the fields of taxation of income and capital and of business and land taxation and its Final Protocol, signed in Luxembourg on 23 August 1958, as amended by the Supplementary Protocol of 15 June 1973 ('the Convention on the avoidance of double taxation between the Grand Duchy of Luxembourg and the Federal Republic of Germany').

5 The Finanzamt set the tax rate at 42% of the taxable income of the branch in accordance with Paragraph 23(2) and (3) of the Law on Corporation Taxation 1991 (Körperschaftsteuergesetz; 'KStG') in the version applicable to the circumstances of the case in the main proceedings.

6 The objection and the action before the Finanzgericht (Finance Court), by which CLT-UFA submitted that that tax rate was discriminatory and that it infringed its right to freedom of establishment under Article 52 of the Treaty read in conjunction with Article 58 thereof, proved unsuccessful. Therefore, CLT-UFA brought an action before the Bundesfinanzhof (Federal Finance Court) seeking annulment of the judgment of the Finanzgericht and amendment of the tax decision in the form of a reduction of the tax rate to 30% of taxable income.

7 The Bundesfinanzhof states that, due to the fact that its seat and central administration are in Luxembourg, CLT-UFA was treated differently and less favourably in respect of its German branch than would have been the case if it had carried on its activity in Germany in the legal form of a limited liability company or public limited company having its seat and/or its central administration in Germany.

8 The Bundesfinanzhof points out that a public limited company which has its seat and/or central administration in Germany would have been subject to corporation tax which, if the profits had been retained, would have been charged at a rate of 45% of the profits before deduction of tax. That high tax rate could, however, have been decreased. Corporation tax could thus have been reduced to 33.5% if the profits distributed to the parent company had been paid over by 30 June 1996 pursuant to Paragraph 27(1) and Paragraph 49(1) of the KStG, point 1 of the first sentence of Paragraph 43(1) and Paragraph 44d(1) of the Law on Income Tax (Einkommensteuergesetz 1994; 'the EStG'). If the profits had been distributed to the parent company after 30 June 1996, the tax rate would have been reduced to 30% of the profits pursuant to the third sentence of Paragraph 44d(1) of the EStG read in conjunction with Paragraph 49(1) of the KStG. The Bundesfinanzhof states that subsidiaries have generally resorted to that facility in order to reduce the tax rate.

9 The Bundesfinanzhof has doubts as to whether the imposition of differing tax rates to the detriment of CLT-UFA is justified. If the tax rate of 42% applied to branches infringes the Treaty the Bundesfinanzhof requests the Court to stipulate the rate which should be applied in order to cure that infringement. The Bundesfinanzhof considers that it would be sufficient to reduce the tax rate on the profits of the place of business of CLT-UFA to 33.5% in so far as that company had profits at its disposal at the end of the financial year in dispute.

The questions referred

10 It is in those circumstances that the Bundesfinanzhof decided to stay the proceedings and refer the following questions to the Court for a preliminary ruling:

'(1) Is Article 52 in conjunction with Article 58 of the EC Treaty to be interpreted as meaning that charging the profits made in 1994 by a capital company from another Member State through a branch in Germany to German corporation tax at the rate of 42% ("the place of business tax rate") constitutes an infringement of the right to freedom of establishment, given that

(a) the profits would have been charged to German corporation tax at the rate of only 33.5% if they had been made by a company subject to unlimited corporation tax in Germany which was a subsidiary of a capital company from another Member State and had distributed all the profits to its parent by the end of 30 June 1996;

(b) the profits would initially have been charged to German corporation tax at the rate of 45% if the subsidiary had retained them until the end of 30 June 1996, but the liability to corporation tax would have been reduced retrospectively to 30% if the profits had been distributed in full after 30 June 1996?

(2) If the place of business tax rate infringes Article 52 in conjunction with Article 58 of the EC Treaty, is it necessary to reduce it to 30% for the financial year in dispute in order to cure the infringement?’

The first question

11 With its first question the national court judge is effectively asking whether Article 52 and Article 58 of the Treaty preclude a national law such as the one in dispute in the main proceedings which, in the case of a branch of a company which has its seat in another Member State, lays down a tax rate on the profits of that branch which is higher than that on the profits of a subsidiary of such a company where that subsidiary distributes its profits in full to its parent company.

12 It must be remembered that Article 52 of the Treaty constitutes one of the fundamental provisions of Community law and has been directly applicable in the Member States (see, in particular, Case C-307/97 *Saint-Gobain ZN* [1999] ECR I-6161, paragraph 34).

13 Under that provision, freedom of establishment for nationals of one Member State on the territory of another Member State includes the right to take up and pursue activities as self-employed persons and to set up and manage undertakings under the conditions laid down for its own nationals by the law of the country where such establishment is effected. The abolition of restrictions on freedom of establishment also applies to restrictions on the setting up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of another Member State (Case 270/83 *Commission v France* [1986] ECR 273, paragraph 13, and Case C-311/97 *Royal Bank of Scotland* [1999] ECR I-2651, paragraph 22).

14 The second sentence of the first paragraph of Article 52 expressly leaves traders free to choose the appropriate legal form in which to pursue their activities in another Member State and that freedom of choice must not be limited by discriminatory tax provisions (*Commission v France*, paragraph 22).

15 Therefore, the freedom to choose the appropriate legal form in which to pursue activities in another Member State primarily serves to allow companies having their seat in a Member State to open a branch in another Member State in order to pursue their activities under the same conditions as those which apply to subsidiaries.

16 In that regard, it must be pointed out that the definitive tax rate of 42% applicable to the profits of branches of parent companies having their seat in another Member State constitutes, generally speaking, unfavourable treatment in relation to the tax rate reduced to 33.5%, or even 30%, which is applicable to the profits of the subsidiaries of such companies.

17 It follows from the above that the refusal to apply the reduced tax rate to branches renders the possibility, for companies having their seat in another Member State, of exercising the right to

freedom of establishment through a branch less attractive. It follows that a national law such as the one in dispute in the main proceedings restricts the freedom to choose the appropriate legal form in which to pursue activities in another Member State.

18 It is thus necessary to examine whether that differential treatment is objectively justified.

19 The Finanzamt and the German Government submit that the differential treatment between branches and subsidiaries relates to situations which are not objectively comparable.

20 They submit in particular that profits, distributed by a subsidiary to its parent company, are no longer assets of the subsidiary, whereas profits transferred by a branch to its head office continue to be part of the internal assets of the same company. According to the German Government and the Finanzamt, that fundamental difference and practical reasons led the national legislature to exclude the application of the reduced tax rate to profits made by branches.

21 The Finanzamt adds that the reduced tax rate applicable to subsidiaries is justified by the fact that tax charged on a subsidiary must be set off against the tax due from the beneficiary parent company, which is subject to unlimited tax in Germany, in order to avoid double taxation of those tax payers.

22 As regards, first, the argument of the German Government and the Finanzamt that there is a fundamental difference between the distribution of profits by a subsidiary to its parent company and the transfer of profits within a company, the Court makes the following observations.

23 In both cases the profits are made available to the company which controls the subsidiary and the branch respectively. The only real difference between the two situations lies in the fact that the distribution of the profits of a subsidiary to its parent company presupposes the existence of a formal decision to that effect, whereas the profits of a branch of a company are part of the assets of that company even in the absence of a formal decision to that effect.

24 In addition, it is apparent from the decision to refer and the observations of the Finanzamt and the German Government that, even if the profits distributed by a subsidiary to its parent company were no longer part of the assets of that subsidiary, those profits could still be made available to that subsidiary by its parent company in the form of share capital or a shareholder loan.

25 Therefore, the fact that profits distributed by a subsidiary to its parent company are no longer part of that subsidiary's assets does not justify the application of a tax rate to the profits of such a subsidiary which is lower than that applied to the same profits made by a branch.

26 As regards the argument of the Finanzamt that the application of the reduced tax rate to subsidiaries is justified in order to avoid the double taxation of tax payers subject to tax primarily in Germany, it must be pointed out that the tax rate does not apply only to profits which are distributed to that category of tax payer. The reduced tax rate also applies to the distribution of profits by German subsidiaries to parent companies having their seat in another Member State, such as in Luxembourg for example.

27 In respect of a German subsidiary of a Luxembourg company, it must also be added that the reduced tax rate which applies to the profits of such a subsidiary, in relation to the rate applicable to the profits of a branch, is not compensated for by applying a higher tax rate to the profits of the Luxembourg parent company.

28 The Bundesfinanzhof states that, by reading together Article 5(1), Article 13(1) and (2), and

Article 20(1) and (2) of the Convention on the avoidance of double taxation between the Grand Duchy of Luxembourg and the Federal Republic of Germany, both the profits of a Luxembourg company made by a German branch and those made by a German subsidiary are exonerated from Luxembourg corporation tax.

29 In the light of the information provided by the Bundesfinanzhof in its decision to refer, it appears, furthermore, that the national legislation on the manner of determining the taxable amount does not draw a distinction between companies with their seat in another Member State, according to whether they pursue their activities through a branch or a subsidiary, which is capable of justifying a difference in treatment between the two categories of companies.

30 In those circumstances, it seems that German subsidiaries and branches of companies having their seat in Luxembourg are in a situation in which they can be compared objectively.

31 In the light of the above considerations, the answer to the first question must be that Article 52 and Article 58 of the Treaty preclude a national law such as the one in dispute in the main proceedings which, in the case of a branch of a company having its seat in another Member State, lays down a tax rate on the profits of that branch which is higher than that on the profits of a subsidiary of such a company where that subsidiary distributes its profits in full to its parent company.

The second question

32 With its second question the Bundesfinanzhof is effectively asking whether a tax rate applicable to the profits of a branch, such as the one in dispute in the main proceedings, must be reduced to 33.5%, which was the rate applicable to profits distributed up until 30 June 1996, or to 30%, namely the rate applicable from that date, in order to be consistent with Article 52 and Article 58 of the Treaty.

33 In that regard, it follows from the answer to the first question that it is necessary to apply a tax rate to the profits made by a branch which is equivalent to the overall tax rate which would have been applicable in the same circumstances to the distribution of the profits of a subsidiary to its parent company.

34 That comparison has to be made in the light of the factual circumstances of the case in the main proceedings.

35 In that regard, it must be noted that in proceedings under Article 234 EC, which is based on a clear separation of functions between the national courts and the Court of Justice, any assessment of the facts in the case is a matter for the national court (see Case 36/79 *Denkavit Futtermittel* [1979] ECR 3439, paragraph 12, Case C-235/95 *Dumon and Froment* [1998] ECR I-4531, paragraph 25, and Joined Cases C-175/98 and C-177/98 *Lirussi and Bizzaro* [1999] ECR I-6881, paragraph 37, and Case C-282/00 *RAR* [2003] ECR I-4741, paragraph 46).

36 The Court thus has no jurisdiction to give a ruling on the facts in an individual case or to apply the rules of Community law which it has interpreted to national measures or situations, since those questions are matters for the exclusive jurisdiction of the national court (see Case 13/68 *Salgoil* [1968] ECR 661; Case 51/74 *Van der Hulst* [1975] ECR 79, paragraph 12; Case C-320/88 *Shipping and Forwarding Enterprise Safe* [1990] ECR I-285, paragraph 11; *Lirussi and Bizzaro*, paragraph 38, and *RAR*, paragraph 47).

37 The answer to the second question must therefore be that it is for the national court to determine the tax rate which must be applied to the profits made by a branch, such as the one in

dispute in the main proceedings, by reference to the overall tax rate which would have been applicable if the profits of a subsidiary had been distributed to its parent company.

Costs

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

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

1. Article 52 of the EC Treaty (now, after amendment, Article 43 EC) and Article 58 of the EC Treaty (now Article 48 EC) preclude a national law such as the one in dispute in the main proceedings which, in the case of a branch of a company having its seat in another Member State, lays down a tax rate on the profits of that branch which is higher than that on the profits of a subsidiary of such a company where that subsidiary distributes its profits in full to its parent company.

2. It is for the national court to determine the tax rate which must be applied to the profits made by a branch, such as the one in dispute in the main proceedings, by reference to the overall tax rate which would have been applicable if the profits of a subsidiary had been distributed to its parent company.

[Signatures]

* Language of the case: German.