

Newsalert

EU Direct Tax Group

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ECJ judgment on the Finnish rules on taxation of non-residents' pension income (case C-520/04, Turpeinen)

The ECJ rendered its judgment in case C-520/04, Turpeinen on 9 November 2006, which concerns Finnish withholding taxation in relation to free movement of persons (Art. 39 EC) and right to reside and move freely within the territory of the Member States (Art. 18 EC). The ruling, which is summarised below, followed very closely the reasoning of AG Léger's opinion of 18.5.2006.

Mrs. Turpeinen, a Finnish national living abroad (first in Belgium and then in Spain) since 1998, was considered non-resident for Finnish tax purposes as from 2002. In 2002 her worldwide income consisted only of Finnish-source pension payments from her earlier public service. The Finnish – Spanish tax treaty assigned taxing rights on this income to Finland. Under Finnish law, such earned income received by non-residents was taxed at the flat rate of 35 %, whereas residents were taxed at progressive rates between 0-55 %. In fact, Turpeinen had in 1999-2001, when still considered resident for Finnish purpose, been levied taxes at 28.5 % on the same income.

The Supreme Administrative Court of Finland (KHO) asked the ECJ whether the Finnish withholding tax legislation is contradictory to Articles 18 and 38 EC or alternatively Directive 90/365/EC especially in a situation like this, where the person claiming the benefits of the EC Treaty is a person, without economic cross-border nexus, receiving pension payments from her earlier public service.

Firstly, the ECJ considered which of the EC Treaty freedoms (Art. 39 or Art. 18 EC), should be applied in this case. Referring to AG Léger's opinion the Court concluded that Art. 39 EC does not apply since Turpeinen was not, and in fact had never been, working outside Finland. Accordingly, the case was analyzed from the perspective of Art. 18 EC, because it gave Turpeinen the right to reside and move freely within the EU and prohibited also home state exit restrictions on such movements.

When analysing the Finnish rules under Art. 18 EC, the ECJ concluded that Turpeinen, as a non-resident, had been taxed more heavily than residents on similar income. Following this, the ECJ, however, first pointed out that residents and non-residents are not in comparable situation from the point of view of the source of their income and of their personal ability to pay and family/personal circumstances. However, the ECJ went on and applied the "Schumacker-rule" to the case. When doing this, it stated that, in so far as the pension paid in Finland constitutes all or almost all of their income, non-residents retired persons like Ms Turpeinen are, objectively speaking, in the same situation as regards income tax as retired persons resident in Finland. In such a case, the different treatment could be justified only if there were objective considerations proportionate to the legitimate aim of the national provisions.

The Court, however, rejected all of the presented attempts to justify the different treatment. The ECJ also pointed out that the relevant Finnish tax provisions had actually been meanwhile changed so that all Finnish-source pension income is taxed as if the recipient was resident for Finnish purposes, regardless his state of residence. On those grounds, the ECJ ruled that "Article 18 EC must be interpreted as meaning that it precludes national legislation according to which the income tax on a retirement pension paid by an institution of the Member State concerned to a person residing in another Member State exceeds in certain cases the tax which would be payable if that person resided in the first Member State, where that pension constitutes all or nearly all of that person's income."

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