Tax Treaties After the BEPS Project
A Tribute to Jacques Sasseville

Edited by Brian J. Arnold

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Interpretation of Tax Treaties by the Court of Justice of the European Union

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The Background to the Judgment of the Court of Justice of the European Union with Respect to Article 25(5) of the Austria-Germany Treaty

On September 12, 2017, the Court of Justice of the European Union (CJEU) issued its first judgment with respect to article 25(5) of the Austria-Germany treaty, which reads as follows:

> In the case of difficulties or doubts concerning the interpretation or the application of this convention, for which no solution can be found during a mutual agreement procedure between the competent authorities arranged in accordance with the preceding paragraphs of this article within a period of three years from the initiation of that procedure, the States Parties are obliged, at the request of the person referred to in paragraph 1, to submit the dispute to the Court of Justice of the European Communities under an arbitration procedure pursuant to Article [239 of the EC treaty].[1]

Article 239 of the EC treaty,[2] which is mentioned in article 25(5) of the Austria-Germany treaty, and was later incorporated into article 273 of the Treaty on the Functioning of the European Union (TFEU), reads: "The Court of Justice shall have jurisdiction in any dispute between Member States which relates to the subject

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1 The Convention Between the Republic of Austria and the Federal Republic of Germany for the Avoidance of Double Taxation with Respect to Taxes on Income and on Capital and to Trade Tax and Land Tax, signed at Berlin on August 24, 2000 (herein referred to as "the Austria-Germany treaty"), quoted in *Austria/Germany* (September 12, 2017), C-648/15, at paragraph 8 (CJEU).

2 Consolidated versions of the Treaty Establishing the European Community, OJ C 325, October 24, 2002, article 239 (herein referred to as "the EC treaty").

matter of the Treaties if the dispute is submitted to it under a special agreement between the parties."[3] Although several tax treaties contain rules with respect to arbitration procedures, a provision such as article 273 that designates the CJEU as the arbitration court for treaty issues is unique.

Article 25(5) of the Austria-Germany treaty was developed in 1997 as part of a research project carried out at the Institute for Austrian and International Tax Law of the Vienna University of Economics and Business (WU Vienna).[4] The project led to the drafting of a model provision for a treaty rule, which refers to article 273 of the TFEU.[5] The draft provision was included, with little modification, in the treaty concluded between Austria and Germany in 2000; the treaty entered into force on August 18, 2002. More than 15 years passed before the CJEU was asked to issue a judgment on article 25(5).

The facts of the case are as follows. Between 1996 and 1998, Bank Austria AG, established in Austria, purchased certificates from the Westdeutsche Landesbank Girozentrale Düsseldorf und Münster (now Landesbank NRW), which had its registered offices in Germany. The conditions for the issuance of the certificates were:

- The certificates conferred entitlement to an annual payment at a fixed percentage of their nominal value.
- If the annual payment was likely to give rise to an accounting loss, its amount was reduced accordingly.
- However, the certificates conferred entitlement, during the period of their existence, to the payment of arrears over the course of subsequent years, provided that the adjustment did not give rise to an accounting loss.
- The payment of interest and the payment of arrears had priority over allocations to reserves and payments to guarantors.
- The amount of capital made available to the issuer in return for the certificates was reimbursed at the nominal value of those certificates.
- However, if the balance sheet showed a loss, the amount of the claim for reimbursement was reduced accordingly. In that case, too, the difference as

3 Consolidated versions of the Treaty on European Union and the Treaty on the Functioning of the European Union, OJ C 326, October 26, 2012, article 273 (herein referred to as "the TFEU").

4 Mario Züger, "Mutual Agreement and Arbitration Procedures in a Multilateral Tax Treaty," in Michael Lang, Helmut Loukota, Albert J. Rädler, Josef Schuch, Gerald Toifl, Christoph Urtz, Franz Wassermeyer, and Mario Züger, eds., *Multilateral Tax Treaties: New Developments in International Tax Law* (The Hague: Kluwer Law International, 1998), 153-86, at 176 et seq.; Mario Züger, *Schiedsverfahren für Doppelbesteuerungsabkommen: Möglichkeiten zur Verbesserung des Rechtsschutzes im Internationalen Steuerrecht* (Vienna: Linde, 2001), at 123; and Mario Züger, "Der EuGH als Schiedsgericht im Neuen DBA Österreich-Deutschland" (1999) *Steuer und Wirtschaft International* [*Tax and Business Review*] 9, at 20.

5 Michael Lang, "Überlegungen zur Österreichischen DBA-Politik" (2012) *Steuer und Wirtschaft International* [*Tax and Business Review*] 108-27, at 111; and Klaus Lehner and H.C. Lehner, *Doppelbesteuerungsabkommen: DBA*, 6th ed. (Munich: Beck, 2015), article 25, at paragraph 268.

compared with the nominal value of the certificates was made up over the course of subsequent years, provided that the adjustment did not give rise to an accounting loss.
- The certificates conferred no right to participate in the proceeds from the winding up of the issuing company.
- The issuing company had a right to cancel if the certificates no longer gave rise to tax deductibility.[6]

The Austrian and German tax authorities disagreed whether the interest on the certificates was subject to article 11(1) or article 11(2) of the Austria-Germany treaty. According to article 11(1), interest may be taxed only in the residence state of the beneficial owner. Article 11(2) states that "income from rights or debt-claims with participation in profits, including income received by a silent partner from his participation as a silent partner or income from profit-participating loans and profit-sharing bonds, may . . . also be taxed in the State Party in which it arises, in accordance with the laws of that State."[7] The Austrian tax authorities claimed that the certificates at issue were not rights that granted participation in profits within the meaning of article 11(2) of the Austria-Germany treaty, whereas the German tax authorities took the contrary view. Thus, according to Austria, Austria had the sole right to tax under article 11(1), whereas, according to Germany, article 11(2)(b) authorized Germany to impose taxation and, moreover, article 23(2)(b) obliged Austria to give credit for the German tax. These divergent views on the legal characterization of the interest received by Bank Austria prompted the two states to claim the right to tax that interest, thus leading to double taxation for Bank Austria in the financial years between 2003 and 2009.

Pursuant to article 25(1) of the Austria-Germany treaty, Bank Austria lodged a request to initiate the mutual agreement procedure with the Austrian tax authorities. That procedure was initiated by the Austrian Ministry of Finance, but ended in an acknowledgment of failure in 2011. Bank Austria then asked the Austrian tax authorities to submit the dispute to the CJEU in accordance with article 25(5) of the Austria-Germany treaty.

The Jurisdiction of the CJEU

The CJEU confirmed its jurisdiction under article 273 of the TFEU,[8] a position that had already been justified in scholarly legal writings. The court did not have any doubts as to the existence of a dispute between the states:

6 *Austria/Germany*, supra note 1, at paragraph 12.

7 Austria-Germany treaty, supra note 1, at article 11(2).

8 See Mario Züger, "Der Einfluss des Schiedsverfahren vor dem EuGH auf das Abgabenrecht," in Michael Holoubek and Michael Lang, eds., *Das EuGH-Verfahren in Steuersachen* (Vienna: Linde, 2000), 301-20, at 304 et seq.; Züger, "Der EuGH als Schiedsgericht im Neuen DBA Österreich-Deutschland," supra note 4, at 21 et seq.; and Züger, *Schiedsverfahren für Doppelbesteuerungsabkommen*, supra note 4, at 125.

> The Republic of Austria and the Federal Republic of Germany both claim the exclusive right to tax income relating to financial years in which those two States were members of the European Union. Those concurrent claims led, in so far as concerns the taxable person, to double taxation contrary to the aims of the Austro-German Convention, by which the States Parties to that convention sought specifically to avoid double taxation. Since the mutual agreement procedure provided for by that convention was unsuccessful, the existence of a dispute between Member States within the meaning of Article 273 TFEU must be regarded as established.[9]

In contrast, the court's jurisdiction is conditional on the dispute being related to the subject matter of the treaty:

> As the Advocate General stated in point 43 of his Opinion, it follows from a comparison of the various language versions of Article 273 TFEU that the phrase "related to" must be understood as a link rather than a requirement that the subject matter be the same.
>
> That interpretation is supported by a comparison with the faculty, laid down in Article 259 TFEU, for a Member State to bring an action for failure to fulfil obligations against another Member State when it considers that the latter has failed to fulfil one of its obligations under the Treaties themselves.
>
> The condition laid down in Article 273 TFEU that the dispute should be related to the subject matter of the treaties is therefore satisfied when it is established that the dispute brought before the Court has an objectively identifiable link with the subject matter of the Treaties.
>
> That is manifestly so in the present case, in the light of the beneficial effect of the mitigation of double taxation on the functioning of the internal market that the European Union seeks to establish in accordance with Article 3(3) TEU and Article 26 TFEU.[10]

Interestingly, the CJEU did not base its decision exclusively on primary legislation, but also on a statement of the European Commission, which

> observed, in essence, in its communication to the European Parliament, the Council and the European Economic and Social Committee of 11 November 2011, entitled "Double Taxation in the Single Market" (COM(2011) 712 final), the purpose and effect of the conclusion between two Member States of a convention avoiding double taxation is to eliminate or mitigate certain consequences resulting from the uncoordinated exercise of their powers of taxation, which is, by its nature, capable of restricting, discouraging or rendering less attractive the exercise of the freedoms of movement provided for in the TFEU.[11]

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9 *Austria/Germany*, supra note 1, at paragraph 21.

10 Ibid., at paragraph 23 et seq.

11 Ibid., at paragraph 26.

Previously, a primary legislation provision, article 293 of the EC treaty, explicitly addressed this objective: "Member States shall, so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals . . . the abolition of double taxation within the Community."[12] However, article 293 was not incorporated into the TFEU.[13]

Finally, the CJEU examined whether article 25(5) of the Austria-Germany treaty constituted a "special agreement" under article 273 of the TFEU:

> It is true that this application was not lodged pursuant to an arbitration clause specifically adopted with a view to resolving the dispute, but pursuant to a general term of the Austro-German Convention, namely, Article 25(5) thereof, before that dispute arose, by which the States Parties undertook to bring before the Court all difficulties which could arise concerning the interpretation or the application of that convention not resolved by amicable agreement.
>
> However, in the light of the objective pursued by Article 273 TFEU, which consists in affording the Member States a means of resolving those of their disputes which relate to the subject matter of the Treaties within the framework of the EU judicature, there is no reason for the parties not to acknowledge, before a dispute arises, an agreement on the referral to the Court of any potential dispute in predefined circumstances in a provision such as Article 25(5) of the Austro-German Convention (see, to that effect, judgment of 27 November 2012, *Pringle*, C-370/12, EU:C:2012:756, paragraph 172).
>
> The Court has therefore jurisdiction to rule on this dispute.[14]

The Importance of the Interpretation Rule in Article 3(2) of the OECD Model Convention

In the *Austria/Germany* case, the CJEU had to address the question whether the remuneration from the certificates was to be regarded as "participation in profits" within the meaning of article 11(2) of the Austria-Germany treaty. The term is not defined in the treaty. The CJEU pointed out that the Federal Republic of Germany "relies on the interpretation of the concept under its national law, in particular on a judgment of the Bundesfinanzhof (Federal Finance Court, Germany) of 26 August 2010, according to which the remuneration from the certificates at issue is to be regarded as participation in profits."[15] Subsequently, the court examined the interpretation provision in the Austria-Germany treaty, which is modelled

12 Supra note 2, article 293.

13 See Moris Lehner, "Beseitigt die neue Verfassung für Europa die Verpflichtung der Mitgliedstaaten zur Vermeidung der Doppelbesteuerung?" (2005) 12 *IStR* 397.

14 *Austria/Germany*, supra note 1, at paragraphs 27-30.

15 Ibid., at paragraph 34; see Bundesfinanzhof judgment of August 26, 2010, IR 53/09.

on article 3(2) of the OECD model convention:[16] "Indeed, Article 3(2) of the Austro-German Convention sets out a rule of interpretation according to which a term or phrase not defined by that convention must be given the meaning it has under the tax law of the State applying it."[17]

At first glance, the CJEU gives the impression that it interprets article 3(2) of the treaty as enshrining the relevance of national law for the interpretation of the treaty, largely because it refrains from quoting the phrase "unless the context otherwise requires" contained in article 3(2) of both the OECD model convention and the Austria-Germany treaty. The following sentences in its judgment, however, correct this initial impression:

> Nevertheless, such a rule of interpretation by a single State at a given point in time is not to be regarded as a rule intended to arbitrate between divergences of interpretation between the two States Parties.
>
> A construction to the contrary would, furthermore, deprive of all practical effect the provisions of Article 25(5) of that convention, whose mutual agreement procedure and clause conferring jurisdiction on the Court would have scarcely any meaning if the States Parties had intended that convention to be interpreted only by reference to national laws alone, even when, as in the present case, those laws have diametrically opposed implications.[18]

The CJEU thus held that an interpretation of article 3(2) of the Austria-Germany treaty that regards the national law of the contracting states as relevant for terms not defined in the treaty itself would not be in accordance with the object and purpose of the treaty. "Divergences of interpretation" of the treaty—specifically, cases of double taxation that arise from different interpretations of the same convention provision—cannot be avoided in this manner.[19] It is interesting to note that the CJEU also invoked article 25(5) of the Austria-Germany treaty in this regard. The CJEU rightly held that the states parties cannot have intended the convention to be interpreted only by reference to national laws when those laws have "diametrically opposed implications." The CJEU's reference to article 25(5) of the treaty must not, however, be understood as meaning that an autonomous interpretation is limited to article 3(2) of the Austria-Germany treaty, since the court mentioned not only article 25(5) of this treaty but also the "mutual agreement procedure." Rules with respect to the mutual agreement procedure are found

16 Organisation for Economic Co-operation and Development, *Model Tax Convention on Income and on Capital: Condensed Version 2014* (Paris: OECD, July 2014) (herein referred to as "the OECD model convention"). The 2017 update to the OECD model convention was published in November 2017.

17 *Austria/Germany*, supra note 1, at paragraph 35.

18 Ibid., at paragraphs 36-37.

19 Ibid., at paragraph 36.

in both article 25 of the Austria-Germany treaty and article 25 of the OECD model convention. It is thus arguable that the CJEU might interpret other conventions that contain a provision modelled on article 3(2) of the OECD model convention according to the same principles.

The question remains whether the CJEU would accept an interpretation based on national law in accordance with article 3(2) where an undefined term in the treaty is understood in the same manner in both contracting states. The CJEU was not asked to decide this question and, as a result, the court was at least able to reject an interpretation according to national law where such an interpretation leads to conflicting interpretations in the two states. In any event, the relevance of national law is not logical even where the term used in a treaty—identical to the term used in the OECD model convention—has the same meaning in both contracting states. After all, when the contracting states incorporate a provision of the OECD model convention in a bilateral treaty, it can be assumed that their intention was to adopt the meaning of the term in the OECD model convention.[20]

The CJEU also (obviously) assumed that both contracting states "apply" the treaty in accordance with article 3(2) of the Austria-Germany treaty, and thus also in accordance with article 3(2) of the OECD model convention. Otherwise, the court would not have been concerned that an interpretation based on national law might lead to "diametrically opposed implications." The CJEU thus implicitly rejected[21] the interpretation preferred by John Avery Jones et al.[22] according to which only the source state applies the convention and therefore both contracting states must rely on the meaning of the term given by the law of the source state.

In this particular case, however, it is doubtful whether Germany actually advocated an interpretation of article 3(2) of the treaty that favoured the relevance of national law. The CJEU judgment stated: "In that regard, the Federal Republic of Germany relies on the interpretation of the concept under its national law, in particular on a judgment of the Bundesfinanzhof (Federal Finance Court,

20 See Michael Lang, "Überlegungen zur österreichischen DBA-Politik," supra note 5, at 123; see also Michael Lang, "Die Bedeutung des Musterabkommens und des Kommentars des OECD-Steuerausschusses für die Auslegung von Doppelbesteuerungsabkommen," in W. Gassner, Michael Lang, and E. Lechner, eds., *Aktuelle Entwicklungen im Internationalen Steuerrecht: Das neue Musterabkommen der OECD* (Vienna: Linde, 1994), 11, at 23.

21 Similarly, Michael Lang, "Die Bedeutung des Originär Innerstaatlichen Rechts für die Auslegung von Doppelbesteuerungsabkommen (Art. 3 Abs. 2 OECD-MA)," in G. Burmeister and D. Endres, eds., *Außensteuerrecht, Doppelbesteuerungsabkommen und EU-Recht im Spannungsverhältnis: Festschrift für Helmut Debatin zum 70. Geburtstag* (Munich: Beck, 1997), 283, at 286.

22 John F. Avery Jones, Charles J. Berg, Henri-Robert Depret, Maarten J. Ellis, Pierre Fontaneau, Raoul Lenz, Toshio Miyatake, Sidney I. Roberts, Claes Sandels, Jakob Strobl, and David A. Ward, "The Interpretation of Tax Treaties with Particular Reference to Article 3(2) of the OECD Model: Part 1" [1984] no. 1 *British Tax Review* 14-54, at 50 and 54.

Germany) of 26 August 2010, according to which the remuneration from the certificates at issue is to be regarded as participation in profits."[23]

The court thus understood the reference to the judgment of the Bundesfinanzhof as a reference to national law. In the cited judgment, however, the Bundesfinanzhof did not interpret a provision of national law but, rather, the provisions of article 11(2) of the Austria-Germany treaty, which were also relevant in the CJEU's decision. In its judgment, the Bundesfinanzhof explicitly rejected the relevance of national law for the interpretation of the convention:

> Since the remunerations at issue must be qualified as interest with participation in profits according to an autonomous interpretation of the DTC [the Austria-Germany treaty], neither the interpretation of the term of the right of participation in profits within the meaning of Section 8(j3)(2) Corporate Income Tax Act . . . nor the distinction criteria for certificates under national civil law put forward by the Plaintiff in connection with Section 221(3) of the German Stock Corporation Act are relevant.[24]

Even the advocate general had not considered the Bundesfinanzhof judgment in his opinion, albeit on the basis of different arguments:

> That conclusion cannot be altered by the fact, on which the Federal Republic of Germany relies heavily in its written submissions, that the Bundesfinanzhof (Federal Finance Court, Germany) arrived at a contrary conclusion in a judgment of 26 August 2010. In the context of the application of Article 273 TFEU, the Court cannot be bound by assessments carried out by a Court of one of the Member States party to the dispute, at the risk of depriving of all practical effectiveness the arbitration clause under which those States chose to entrust the Court with the settlement of that dispute. In the present case, since that clause concerns the interpretation and application of the German-Austrian Convention, the Court is, of course, entirely at liberty to interpret that convention in the light of the principles of interpretation flowing from the Vienna Convention on the Law of Treaties.[25]

The fact that the CJEU is not "bound" by assessments carried out by a court of a member state is undisputed, but that should not have prevented the court from addressing the reasons given by the Bundesfinanzhof and explaining why those reasons were not convincing. Unfortunately, the CJEU refrained from addressing the arguments that were considered relevant by the Bundesfinanzhof.

However, the CJEU was correct in concluding that "[t]he concept of 'debt-claims with participation in profits,' for the purpose of the Austro-German Convention must, therefore, be interpreted according to the methods proper to international law":[26]

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23 *Austria/Germany*, supra note 1, at paragraph 34.

24 See Bundesfinanzhof judgment of August 26, 2010, IR 53/09, supra note 15, at paragraph 25.

25 Opinion of the advocate general in *Austria/Germany* (April 27, 2017), C-648/15, at paragraph 107.

26 *Austria/Germany*, supra note 1, at paragraph 38.

> In that regard, it should be borne in mind that it follows from the provisions of the Vienna Convention, to which both the Republic of Austria and the Federal Republic of Germany are parties, that a treaty must be interpreted in good faith in accordance with the ordinary meaning to be given to its terms in their context and in the light of its object and purpose, taking into account any relevant rules of international law applicable in the relations between the parties to that treaty (see, to that effect, judgment of 25 February 2010, *Brita*, C-386/08, EU:C:2010:91, paragraph 43).[27]

The Interpretation of the Term "Participation in Profits"

In interpreting the term "participation in profits" in article 11(2) of the Austria-Germany treaty, the CJEU began with the wording:

> As regards, first of all, the ordinary meaning to be given to the terms "participation in profits," both everyday language and the most commonly accepted accounting conventions refer to an acceptance which implies, in principle, the object of receiving a share in the positive income of the annual operations of an undertaking. That is generally the case of a shareholder but also, in particular, of an employee whose employment contract provides for a bonus representing a proportion of the profits realised by the employer.
>
> Furthermore, the phrase "participation in profits" is normally associated with the inherent variability and unpredictability of the annual income of any high-risk economic activity. Thus, participation in the profits of a financial year generally implies the right to receive an amount that is uncertain at the beginning of the financial year, that is liable to vary from one year to another and is indeed capable of being zero.
>
> The phrase "debt-claims with participation in profits" therefore refers to financial products the remuneration of which varies, at least partially, according to the debtor's annual profits.[28]

It is surprising that the court attached great importance to the wording of article 11(2), especially when compared with the rest of its reasoning. The "everyday language" mentioned by the CJEU does not have much to offer in the context of sophisticated financial products, where technical business terminology is more appropriate. Nor does the judgment contain any further evidence on the "commonly accepted accounting conventions" cited by the court. Finally, with respect to this part of its judgment, one could reproach the CJEU for putting forward allegations instead of arguments.

Moreover, in analyzing the purpose of the provisions of which the phrase "debt-claims with participation in profits" forms part, the court noted

> that Article 11(2) of the Austro-German Convention appears as a derogation from the principle, expressed in Article 11(1) of that convention, of allocating between the States

27 Ibid., at paragraph 39.

28 Ibid., at paragraphs 40-42.

> Parties their powers of taxation on the basis that interest is, in principle, taxed only in the State of establishment or residence of its beneficiary. That derogation enables interest earned on a debt-claim with participation in profits to be taxed "also" in the State of its source. It is therefore for the State of the establishment or residence of the beneficiary of that interest to offset the double taxation by deducting the tax already levied at the source from the other tax owed by the holder of the debt-claim.
>
> Having regard to the general scheme and purpose of the Austro-German Convention, which consists in avoiding, as far as possible, legal double taxation in cross-border situations between the two States Parties, the criterion allowing for derogation from the agreed allocation of powers of taxation, namely there being participation in profits, must be given a strict interpretation.[29]

This line of reasoning of the CJEU is also vulnerable to criticism. The CJEU assumes that derogations must be given a strict interpretation and it often takes this position in its judgments,[30] but that does not make it any more convincing. Instead, its position becomes methodologically untenable. After all, it is merely a question of legal technique whether one broadly formulates a regulation at the beginning, only to restrict it later with an exemption provision, or whether one narrowly defines it from the outset.[31] Legislative coincidences such as this should not have any influence on the result of the interpretation. In addition, assumptions about which provisions apply as a rule and which apply as exceptions are largely arbitrary. That is the case here: it would be equally possible to regard national laws, which postulate a tax obligation for income from debt-claims with participation in profits, as being the rule. The exemption in article 11(1) of the Austria-Germany treaty would then be the exception and, in turn, article 11(2) of the treaty would be the provision that confirms the basic rule. From this equally legitimate perspective, according to the methodological premises of the CJEU, article 11(1) of the Austria-Germany treaty should then be given a strict interpretation, while article 11(2) should not.

Another consideration of the CJEU is also interesting:

> A broad interpretation of the phrase "participation in profits" referred to in Article 11(2) of the Austro-German Convention would be liable to limit the scope of Article 11(1) thereof, which, by a strict division of powers of taxation of interest, is intended to avoid any double taxation, whereas an application of Article 11(2) implies double taxation, the detrimental effects of which on the proper functioning of the internal market are

29 Ibid., at paragraphs 48-49.

30 See Michael Potacs, *Auslegung im öffentlichen Recht* (Baden-Baden: Nomos, 1994), at 79 et seq.

31 Hans Georg Ruppe, *Die Ausnahmebestimmungen des Einkommensteuergesetzes: Probleme der Rechtsanwendung und Rechtsfortbildung bei den "Steuerbegünstigungen" der österreichischen Einkommensteuer* (Vienna: Orac, 1971), at 28 et seq.; Gerold Stoll, *Das Steuerschuldverhältnis in Seiner Grundlegenden Bedeutung für die Steuerliche Rechtsfindung* (n.p., 1972), at 104; and Michael Lang, *Doppelbesteuerungsabkommen und Innerstaatliches Recht* (Vienna: Orac, 1992), at 75.

mitigated only by the offsetting rule laid down in Article 23(1)(b) and (2)(b) of that convention.[32]

Putting forward the argument of "detrimental effects on the proper functioning of the internal market" in such a case is by no means self-evident. According to article 273 of the TFEU, the CJEU has jurisdiction to settle a dispute between the member states under a special agreement. Contrary to a preliminary ruling procedure, for example, the court does not have the competence to decide whether a rule of national law, interpreted by a national court, conforms with EU law. Therefore, one must ask the question whether the CJEU may allow EU law to be considered at all in the interpretation of a tax treaty provision. The assumption that in its interpretation of the treaty provision the CJEU must consider arguments different from those considered by the national authorities and courts is anything but obvious, since it would mean that the meaning of a treaty provision depends on who the respective interpreter is. If this result is to be avoided, all legal practitioners should, like the CJEU, take EU law into account in the interpretation of tax treaty provisions. This is conceivable where a provision of a treaty between member states, as in this particular case, does not correspond to the OECD model convention. It would be more difficult to imagine, however, if the particular provision were contained in the OECD model convention and incorporated in a bilateral treaty. By incorporating a specific rule of the OECD model convention in their treaty, both contracting states express their intention to include that rule in the treaty; in other words, they want the content of the provision to be identical to that of other bilateral treaty provisions that use the same OECD rule.[33] These other treaties may also be concluded between states that are not members of the EU. There is little room for an interpretation of such treaties in conformity with EU law, and this might cause the contents of identical bilateral tax treaty rules to drift apart. A violation of EU law would thus render the treaty rule inapplicable.

It is not clear why "an application of Article 11(2) implies double taxation, the detrimental effects of which on the proper functioning of the internal market are mitigated only by the offsetting rule laid down in Article 23(1)(b) and (2)(b) of that convention."[34] The CJEU obviously assumes that the link between withholding tax and the credit method as a consequence of the application of article 11(2) in conjunction with article 23(1)(b) of the treaty has "detrimental effects on the proper functioning of the internal market." This assumption may simply be based on the premise that, from the point of view of EU law, the avoidance of double

32 *Austria/Germany*, supra note 1, at paragraph 50.

33 Michael Lang, "Die im Neuen DBA Österreich-Deutschland Enthaltenen Auslegungsregeln," in Wolfgang Gassner, Michael Lang, and E. Lechner, eds., *Das neue Doppelbesteuerungsabkommen Österreich-Deutschland: Der Entwurf im Lichte der österreichischen und deutschen Abkommenspraxis* (Vienna: Linde, 1999), 59, at 72.

34 *Austria/Germany*, supra note 1, at paragraph 50.

taxation through exemption in the source state must be given preference over the credit method. This is the first such statement in the case law of the CJEU. Previously, taxation in the source state and the crediting of this tax in the state of residence were considered problematic (or at least as requiring justification from the perspective of EU law) only when the levying of a withholding tax on the income of non-residents, as opposed to residents in the source state, resulted in unequal treatment,[35] or when unrelieved taxation from the application of the credit method in the state of residence resulted in discrimination against foreign income compared with domestic income.[36] For the first time, the CJEU now clearly considers the credit method to be generally detrimental to "the proper functioning of the internal market." Yet the court provided no reasons for its position.

Let us continue with this train of thought. If, by way of interpretation in conformity with EU law, the CJEU limits the scope of application of the credit method in favour of exemption in the source state, this can only mean that the CJEU believes that the credit method is contrary to EU law. After all, an interpretation in conformity with EU law is admissible only if one of the proposed methods of interpretation is in violation of EU law. The assumption that an interpretation is *more likely* to be reconciled with the provisions of EU law is not admissible. An envisaged interpretation can only *comply with* or *be contrary to* EU law: tertium non datur. Only where an interpretation contradicts EU law will this be taken into account in the interpretation procedure and possibly result in another interpretation (in conformity with EU law) being given preference over it. If an interpretation in conformity with EU law proves inadmissible—for example, because of its stronger grammatical, teleological, or other systematic arguments that, in a particular case, point in a different direction and carry greater weight owing to their persuasiveness—it must be assumed that the provision is in violation of EU law.[37] If this is true with respect to article 11(2) of the Austria-Germany treaty, the consequence would be that article 11(2) as a whole—beyond debt-claims with participation in profits—would be in violation of EU law and thus inapplicable. However, the CJEU itself did not draw this far-reaching conclusion, which boils down to the unlawfulness of the credit method under EU law, but is unavoidable given the assumptions made by the CJEU in this judgment.

35 See, for example, *Gerritse* (June 12, 2003), C-234/01, at paragraph 52 et seq. (CJEU); *X* (October 18, 2012), C-498/10, at paragraph 34 (CJEU); and *Strojírny Prostějov and ACO Industries Tábor* (June 19, 2014), C-53/13 and C-80/13, at paragraph 60 (CJEU).

36 See, for example, *Manninen* (September 7, 2004), C-319/02, at paragraph 55 (CJEU); and *Haribo Lakritzen Hans Riegel* (February 10, 2011), C-436/08, at paragraph 80 et seq. (CJEU).

37 See Michael Lang, "Der Anwendungsvorrang der Grundfreiheiten auf dem Gebiet des Steuerrechts," in Klaus Tipke, Roman Seer, Joanna Hey, and Joachim Englisch, eds., *Festschrift für Joachim Lang, Gestaltung der Steuerrechtsordnung* (Cologne: Otto Schmidt, 2010), 1003, at 1004 et seq.

In justifying its interpretation, the CJEU followed the scheme of article 11(2) of the Austria-Germany treaty:

> Next, as regards context, it should be noted that that concept appears in Article 11(2) of the Austro-German Convention before a list intended to illustrate its meaning, which includes three types of financial instrument the common characteristic of which is . . . that their remuneration is supposed to vary according to the annual profits of the issuer.
>
> The same applies to "profit-sharing bonds," which are generally defined as obligations conferring entitlement to a portion of the issuer's profits, in addition to the fixed interest which they provide.
>
> Similarly, "profit-participating loans" are generally characterised by a fixed or variable base interest rate, supplemented by interest linked to the amount of the debtor's profits.
>
> As to a "silent partner," regardless of the form taken, he is by definition intended to share in the profits of the undertaking in which he holds a stake, as the Republic of Austria indeed claims, without being contradicted.[38]

The fact "that the certificates at issue are remunerated annually on the basis of a fixed percentage of their nominal value, which is itself fixed,"[39] led the CJEU to conclude that "the concept of 'debt-claims with participation in profits' referred to in Article 11(2) of the Austro-German Convention must be interpreted as excluding certificates such as those at issue in the present case."[40]

The Bundesfinanzhof also based its judgment on the list of other instruments in article 11(2) of the treaty, but it came to the diametrically opposite conclusion:

> The previous instance rightly points out that a participation in the profits can only be generally affirmed if the payment that the holder of the debt-claim can demand depends directly or even only indirectly on the amount of the profits. This broad interpretation of the term "participation in profits" is underpinned by a comparison with the examples cited in Article 11(2) of the DTC-Austria 2000 for income received by a silent partner from his participation as a silent partner or income from profit-participating loans and profit-sharing bonds. Even these methods of financing do not necessarily contain an unlimited and direct participation in the profits of the undertaking, but can be based on a participation in profits limited to a certain percentage of the paid-out contribution or the outstanding loan. Therefore the assumption of a participation in profits within the meaning of Article 11(2) DTC-Austria 2000 does not require an orientation toward profits in such a manner that the benchmark for the payment is necessarily the dividend of the shareholders, the annual net profits, or another balance sheet figure. Even if, as pointed out by the plaintiff, the amount of the accounting profit is shapeable through the creation and reversal of reserves within the limits of

38 *Austria/Germany*, supra note 1, at paragraphs 44-47.

39 Ibid., at paragraph 51.

40 Ibid., at paragraph 54.

> Section 268(1) of the Commercial Code, this does not result in the plaintiff being entitled to a fixed remuneration, but to a variable one within the limits agreed in the certificate conditions. Therefore, participations in profits are in contrast to those remunerations (interest) that do not depend on the presence of profits and must also be paid in case of loss. The mere dependence of the owed remuneration upon profit will thus suffice to assume a participation in profits, which can also be based on accounting profit or loss.
>
> Although in case of dispute the return is generally calculated according to a fixed percentage agreed in Section 2(1) GSB [participation certificate conditions], it is profit-dependent in being subject to a condition that there is an adequate amount of accounting profit. Therefore, the interest may range—depending on the amount of the accounting profit—between zero and the respective highest agreed interest. For this reason, the plaintiff cannot successfully argue that the assumption of a participation in profits is opposed by the fact that the plaintiff only managed to realize less than the agreed interest but not more than it.[41]

Both the CJEU and the Bundesfinanzhof followed the scheme of article 11(2) of the Austria-Germany treaty, but they reached different conclusions. Unfortunately, the CJEU did not even consider the arguments of the Bundesfinanzhof.

Conclusion

More than 15 years after the Austria-Germany treaty entered into force, the CJEU had its first opportunity to issue a judgment with respect to article 25(5) of the treaty. The fact that this provision was not applied for so long does not in any way suggest that it was of little significance. Instead, it demonstrates that article 25(5) had the intended preventive effect.[42] The competent authorities of the states obviously came to an understanding in mutual agreement procedures so as to retain control of the resolution of disputes and thereby avoid losing their jurisdiction to the CJEU. As a result, the decision of the CJEU remains the exception. Indeed, the rare nature of such an arbitration procedure before the CJEU proves that the inclusion of an arbitration clause in the tax treaty was worthwhile.

The CJEU seized the opportunity to officially accept its jurisdiction for the interpretation of the Austria-Germany treaty on the basis of the arbitration clause of article 25(5) of the treaty in accordance with article 273 of the TFEU. In this particular case, the CJEU was asked to interpret article 11(2) of the Austria-Germany treaty. It is no coincidence that the interpretation of a provision that

41 See Bundesfinanzhof judgment of August 26, 2010, IR 53/09, supra note 15, at paragraphs 20-21.

42 See Michael Lang, "Der EuGH als Interpret von Doppelbesteuerungsabkommen," in Jürgen Lüdicke, Jörg Manfred Mössner, and Lars Hummel, eds., *Das Steuerrecht der Unternehmen: Festschrift für Gerrit Frotscher zum 70. Geburtstag* (Freiburg: Haufe, 2013), 365-82, at 380; see also Züger, "Der EuGH als Schiedsgericht im Neuen DBA Österreich-Deutschland," supra note 4, at 25.

does not correspond to a provision of the OECD model convention became the subject of a dispute. With respect to rules derogating from the OECD model convention, legal practitioners have only a few indications of how to interpret such provisions. Moreover, such provisions are often badly formulated.[43] Unfortunately, however, the arguments put forward by the CJEU for the interpretation of article 11(2) prove vulnerable to criticism on a detailed analysis. Given the pioneering nature of the case, it would have been preferable for the court to apply careful attention to its reasoning.

The judgment of the CJEU, however, also contains convincing passages. The court clarified that the provision of the Austria-Germany treaty, modelled on article 3(2) of the OECD model convention, by no means allows for recourse to national law. Instead, the interpretation provisions in accordance with international law are relevant. Therefore, with respect to this particular treaty, article 3(2) of the OECD model convention does not represent an exception to the autonomous interpretation of the provisions of a tax treaty in accordance with the interpretation rules that are proper to international law, but instead confirms it. One can only hope that this part of the court's reasoning will have a lasting impact on tax treaty practices and that the national courts will use it as guidance or at least address it. After all, the CJEU is a court of highest authority, and its administration of justice is closely followed not only in the EU but also beyond it.

43 See Lang, "Überlegungen zur Österreichischen DBA-Politik," supra note 5, at 125 et seq.