

# Derouin: Tax Treaties and Regulation No. 1408/71 – Double or Nothing?

**This article considers the European Court of Justice (ECJ) decision of 3 April 2008 in *Derouin*,<sup>1</sup> with emphasis on the importance of the ruling for social security contributions, the 1968 France–UK tax treaty (the Treaty) and Regulation No. 1408/71 (the Regulation).<sup>2</sup> In this respect, it should be noted that the Treaty and the Regulation follow different rules regarding the allocation of taxation rights and the designation of the applicable national social security legislation, respectively.**

## 1. Introduction

In *Derouin*, the relationship between taxes and social security contributions was in question and, in particular, whether or not the Treaty could influence the rights and obligations included in the Regulation. The Regulation is, inter alia, intended to coordinate the levying of social security contributions imposed on employed and self-employed persons and members of their families moving within the European Community. The French general social security and social debt repayment contributions in question in *Derouin* have a hybrid character. On the one hand, they have the characteristics of taxes and, on the other, they fall within the scope of the Regulation from an EC law perspective. The latter is due to the fact that the two contributions were intended to finance French social security schemes. The Treaty and the Regulation adopted different rules on how the various jurisdictions had to be allocated. The Regulation designates the French social security legislation to apply, whilst the Treaty allocates the taxation right on Mr Derouin's UK-source income to the United Kingdom. The ECJ held that the Member States were free to determine the income on which social security contributions were due and that the Treaty could also be taken into account in determining the base, as the Regulation did not exclude its application.

## 2. The Case

### 2.1. The facts

Philippe Derouin resided in France where he practised as a lawyer in a self-employed capacity, whilst being a partner at Linklaters, a partnership governed by English law. Linklaters had its head office in the United Kingdom, but also had offices in other Member States, including France. Mr Derouin was registered at the Paris Court of Appeal (France) as an *avocat*, and, at the same time, with the Supreme Court of England and Wales as a registered foreign lawyer. He performed his work as a

lawyer as a member of Linklaters' Paris office and was remunerated by receiving a share in Linklaters' profits.

Under the Regulation, the French social security legislation applied to Mr Derouin's taxable income. The Regulation establishes rules both for granting social security benefits and levying social security contributions. As a result, Mr Derouin paid social contributions in France. He was covered by a compulsory sickness insurance scheme in France and registered with the Social Security and Family Allowance Contribution Collection Office, Paris, Paris Region (*Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne*, Urssaf) as a self-employed person.

Social security funds in France have large deficits. To eliminate these and reform the social security system, special contributions were introduced by the French legislature, i.e. the Social Debt Repayment Contribution (*Contribution pour le remboursement de la dette sociale*, CRDS) and the General Social Contribution (*Contribution sociale généralisée*, CSG). The proceeds from these contributions were allocated directly to the social security funds<sup>3</sup> without first being attributed to the general treasury.

The taxes for which Mr Derouin was liable regarding the UK part of his partnership income were governed by the Treaty. For purposes of the Treaty, Mr Derouin per-

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1. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*. Discussed, inter alia, in L. Adamietz and M. Schreier, *Europäisches Wirtschafts- & Steuerrecht* (2008), pp. 195-196; M.-C. Bergerès, "La CSG, la CRDS, le droit communautaire et les conventions de lutte contre les doubles impositions," *Revue de droit fiscal* (2008) Comm. 349, pp. 25-27; and D. Gutmann, "Derouin v Urssaf de Paris – Région parisienne: to what extent may EU Member States convert their social security contributions into taxes for tax treaty purposes?," *British Tax Review* (2008), pp. 625-627.

2. Council Regulation (EC) No. 1408/71 of 14 June 1971 on the application of social security schemes to employed persons, self-employed persons and to members of their families moving within the Community (OJ 1971, L 149/2, OJ, English Special Edition 1971 (II), p. 416). In *Derouin*, the version amended and updated by Council Regulation (EC) No. 118/97 of 2 December 1996 (OJ 1997, L 28/1) as amended by Council Regulation (EC) No. 1606/98 of 29 June 1998 (OJ 1998, L 209/1) applied.

3. The CSG is paid to the National Family Allowance Fund (*Caisse nationale des allocations familiales*), the Old-Age Solidarity Fund (*Fonds de solidarité vieillesse*), the compulsory sickness insurance schemes and the National Solidarity Fund for Independence (*Caisse nationale de solidarité pour l'autonomie*). The CRDS is paid to the Social Debt Redemption Funds (*Caisse d'amortissement de la dette sociale*).

formed his professional services in an independent capacity.<sup>4</sup> The Linklaters partnership and, in particular, the UK office constituted a fixed base that Mr Derouin had regularly available to him in the United Kingdom within the meaning of Art. 14 of the Treaty (independent professional services). As a result, the taxation right on the income that Mr Derouin derived in respect of his independent professional services and that was attributable to the fixed base in the United Kingdom was assigned to the United Kingdom. This could similarly apply to the results attributable to the Linklaters offices established in other countries outside France and the United Kingdom (see 5.).

## 2.2. The dispute

Urssaf calculated the CSG and CRDS on the occupational income that Mr Derouin derived from working at Linklaters' office in France and the share of profits realized by Linklaters in the United Kingdom. Mr Derouin disputed the payment of the CSG and CRDS on his UK-source income on the grounds that they were not social security contributions and should be regarded as taxes. According to Mr Derouin, only income that was effectively taxable in France should be subject to the CSG and CRDS. This was not the case for his UK-source income, as the Treaty allocated the authority to tax that income to the United Kingdom. In contrast, Urssaf argued that the contributions in question were social security contributions, that they fell within the scope of the Regulation, and that they had to be calculated on the whole of Mr Derouin's income, both from France and the United Kingdom. In order to obtain clarification on this matter, the Paris Social Security Tribunal (*Tribunal des affaires de sécurité sociale de Paris*) referred the case to the ECJ<sup>5</sup> and submitted the following preliminary question:

Is Regulation 1408/71 ... to be interpreted as precluding a convention, such as the [Treaty], from providing that income received in the United Kingdom by workers resident in France and covered by social insurance in that State is excluded from the base on which the [CSG] and the [CRDS] levied in France are assessed?

## 2.3. The decision

First, the ECJ concluded that Mr Derouin was a self-employed migrant worker, resident in France and carrying on self-employed activities in both France and the United Kingdom<sup>6</sup> and, accordingly, he fell within Art. 14a(2) of the Regulation. Consequently, Mr Derouin was exclusively subject to the social security legislation of his residence state, i.e. France. Second, the ECJ referred to its previous decisions in two infringement procedures against France and held that the CSG and CRDS fell within the scope of the Regulation.<sup>7</sup> Having concluded that the Regulation applied to both Mr Derouin and the CSG and CRDS, the ECJ held<sup>8</sup> that:

since Regulation No. 1408/71 is a means of coordination and not of harmonisation, Member States have the power to determine the tax base for contributions such as the CGS and the CRDS.<sup>9</sup>

As a result, the ECJ decided that:

a Member State is entitled to forgo, unilaterally or in the context of tax treaty such as the [Treaty], the inclusion in the tax base for contributions such as the CSG and the CRDS of income earned in another Member State by a resident self-employed person in a situation such as that of the applicant in the main proceedings. Although it is established that no provision of Regulation No. 1408/71 prohibits a Member State from calculating the amount of the social contributions of a resident on the basis of his total income (see, to that effect, Nikula, paragraph 31), clearly no provision of that regulation requires it to do so.<sup>10</sup>

## 3. Ratione Personae of the Regulation and the Treaty

According to the ECJ, the objective of the Regulation is to ensure the free movement of employed and self-employed persons within the European Community, whilst respecting the special characteristics of national social security legislation.<sup>11</sup> To this end, in the ECJ's view, the Preamble to the Regulation<sup>12</sup> demonstrates that this regulation upholds the principle of the equality of the treatment of workers under the various national legislation and seeks to guarantee the equality of the treatment of all workers working in the territory of a Member State<sup>13</sup> as effectively as possible and not to penalize workers who exercise their right to free movement.<sup>14</sup> The system established by the Regulation is merely a system of coordination<sup>15</sup> regarding, inter alia, the determination

4. Art. 14 Treaty.

5. The Paris Social Security Tribunal had sought an opinion from the French Supreme (Court *Cour de Cassation*) to resolve the question before submitting the preliminary question to the ECJ. The Supreme Court advised the Tribunal to refer the case to the ECJ.

6. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 21. According to the ECJ, this conclusion was apparent from the order of reference and from all the observations submitted to the ECJ.

7. *Id.*, Para. 22. The Court referred to ECJ, 15 February 2000, Case C-34/98, *Commission of the European Communities v. French Republic* on the CRDS and ECJ, 15 February 2000, Case C-169/98, *Commission of the European Communities v. French Republic* on the CSG. See also C. David, "National Reports: France", *European Taxation Supplement* ("Taxation of Cross-Border Pensions") (December 2001), pp. 34-S-39-S.

8. *Id.*, Paras. 24-25. Reference was made to ECJ, 18 July 2006, Case C-50/05, *Maija T.I. Nikula*, Para. 24 and the case law cited therein, i.e. ECJ, 26 January 1999, Case C-18/95, *F.C. Terhoeve v. Inspecteur van de Belastingdienst Particulieren/Ondernemingen buitenland*, Para. 34 and ECJ, 7 July 2005, Case C-227/03, *A.J. van Pommeren-Bourgondiën v. Raad van bestuur van de Sociale verzekeringsbank*, Para. 39.

9. *Id.*, Para. 26.

10. *Id.*, Para. 27.

11. *Id.*, Para. 24. In this respect, compare the Title of the Regulation ("... on the application of social security schemes to employed persons, to self-employed persons and to the members of their families moving within the Community") and the second and fourth recital in the Preamble to the Regulation ("Whereas the freedom of movement for persons, which is one of the cornerstones of the Community is not confined to employed persons but also extends to self-employed persons in the framework of the freedom of establishment and the freedom to provide services" and "Whereas it is necessary to respect the special characteristics of national social security legislations and to draw up only a system of coordination") (emphasis added).

12. Fifth, sixth and tenth recitals Preamble.

13. The same applies, mutatis mutandis, to self-employed persons like Mr Derouin.

14. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 24.

15. *Id.*, Para. 25.

of the social security legislation for employed and self-employed persons who use their right to freedom of movement of workers<sup>16</sup> and freedom of establishment.<sup>17,18</sup>

Given this perspective, the Regulation, and especially the conflict rules in Title II, only applies to cross-border activities, i.e. the place of activity and the place of residence are situated in different Member States.<sup>19</sup> In the case of Mr Derouin, it would be necessary that he also pursued activities as an employed or self-employed person in the United Kingdom. Mr Derouin, however, performed all his activities in France.<sup>20</sup> The Advocate General's Opinion reveals that Mr Derouin considered that he pursued his professional activities exclusively in France. As a result, Mr Derouin argued that the provisions of the Regulation did not apply, as he had not exercised his right to freedom of movement, i.e. the freedom of establishment.<sup>21</sup> The French government also queried the application of the Regulation.<sup>22</sup> Had Mr Derouin only pursued his professional activity in France and merely derived income from the United Kingdom, this would have deprived him of the status of a self-employed migrant worker.<sup>23</sup>

In this respect, in several decisions, the ECJ has stated that:

just as the description "employed person" or "self-employed person" for the purposes of Articles 1(a) and 2(1) of the regulation depends on the national social security scheme under which the person is insured, "a person who is employed" (or "engaged in paid employment") and "a person who is self-employed" for the purposes of Title II of the regulation should be understood to refer to activities deemed such by the legislation applicable in the field of social security in the Member State in whose territory those activities are pursued.<sup>24</sup>

Accordingly, the United Kingdom's view is, in principle, guiding in characterizing Mr Derouin's UK activities, if any, under Art. 14a(2) of the Regulation. The United Kingdom did not clearly indicate during the preliminary proceedings before the ECJ whether Mr Derouin should be regarded as a self-employed or an employed person under UK social security legislation. Rather, the United Kingdom only confirmed "at the hearing [that it] does not levy any social security contribution on Mr Derouin's income from his work in the United Kingdom".<sup>25</sup> This remark could imply that Mr Derouin should be treated as a self-employed person under UK social security legislation, as Art. 14a(2) of the Regulation designates the social security legislation of the residence Member State to apply to a self-employed person pursuing these activities both in his residence Member State and in another Member State.<sup>26</sup>

The ECJ did not elaborate on the possible non-application of the Regulation to Mr Derouin's case in the absence of the status of a self-employed migrant worker. The Court simply commented that it was apparent from the order of reference and from all the observations submitted that Mr Derouin's status was that of a self-employed migrant worker, resident in France and carrying on a self-employed activity in France and the United Kingdom.<sup>27</sup> Accordingly, Mr Derouin, fell within the

scope of Art. 14a(2) of the Regulation. In accordance with this provision, Mr Derouin was exclusively subject to French legislation.<sup>28</sup> In this respect, the ECJ was not entitled to determine and examine the facts of a case and question the finding of the national court in its order of reference.<sup>29</sup>

16. Art. 39 EC Treaty

17. Art. 43 EC Treaty

18. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 24; ECJ, 9 March 2006, Case C-493/04, *L.H. Piatowski v. Inspecteur van de Belastingdienst Grote Ondernemingen Eindhoven*, Paras. 19 and 20; ECJ, 18 July 2006, Case C-50/05, *Maija T.I. Nikula*, Para. 20; ECJ, 8 March 2001, Case C-68/99, *Commission of the European Communities v. Federal Republic of Germany*, Paras. 22 and 23; and ECJ, 26 May 2005, Case C-249/04, *José Allard v. Institut national d'assurances sociales pour travailleurs indépendants (Inasti)*, Para. 31.

19. Art. 2(1) of the Regulation concerns the provision with respect to the personal scope. This article, as such, does not require the presence of a cross-border element, but it only demands the individual involved to be (1) self-employed, employed or a student, (2) subject to the legislation of at least one Member State and (3) a national of a Member State or stateless or a refugee residing within the territory of a Member State. Nevertheless, the Court held in ECJ, 22 September 1992, Case C-153/91, *Camille Petit v. Office national des pensions*, Para. 10 that the Regulation does "not apply to situations which are confined in all respects within a single Member State." See also E.J.L. Pennings, *Grondslagen van het Europese sociaizekerheidsrecht* (Deventer: Kluwer, 2005), pp. 42-43. In addition, the Court in ECJ, 21 February 1991, Case C-140/88, *G. C. Noij v. Staatssecretaris van Financiën*, Para. 10 held that the conflict rules of Title II (Art. 13 to Art. 17a) of the Regulation is "designed to resolve conflicts of legislation which may arise where, during a single period, the place of residence and the place of employment are not situated in the same Member State".

20. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 12. "It is apparent from the reference that Mr Derouin: ...

- performs all his work as a lawyer for the Paris office;
- is remunerated by receiving a share of the profits made by the partnership ..."

Compare also ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 16.

21. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 36.

22. *Id.*

23. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 12, first dash. It was not under discussion that Mr Derouin had the status of a self-employed worker.

24. ECJ, 30 January 1997, Case C-340/94, *E.J.M. de Jaeck v. Staatssecretaris van Financiën*, Paras. 22 and 23 and ECJ, 30 January 1997, Case C-221/95, *Institut National d'Assurances Sociales pour Travailleurs Indépendants (Inasti) v. Claude Hervein et Hervillier SA*, Paras. 20 and 21.

25. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 34.

26. If Mr Derouin had performed his UK activities in the capacity of an employed person, the UK social security legislation would have been designated to apply to this situation by virtue of Art. 14c(a) of the Regulation.

27. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 38.

28. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 21.

29. Compare ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 37, who stated that, in the context of proceedings under Art. 234 of the EC Treaty, it was not for the ECJ either to determine the facts or to apply the rules of EC law in a particular case or to examine the compatibility of domestic law or a tax treaty with EC law.

It is, however, remarkable that Mr Derouin was regarded as a self-employed migrant worker, whereas he stated and argued that he lacked this status, as he performed these activities exclusively in France.<sup>30</sup> The ECJ left this appreciation to the national court and, as that court, *inter alia*, in its order of reference presupposed that Mr Derouin had to be regarded as a self-employed migrant worker, the application of the Regulation was sufficiently established. Nevertheless, attention should be paid to this issue, as, if the national court had found that Mr Derouin pursued his professional activity in France alone and merely derived income from the United Kingdom, he would have been deprived of the status of self-employed migrant worker. As a result, the Regulation would not apply and the interpretation of EC law given by the ECJ in response to the question referred for a preliminary ruling would have been redundant.<sup>31</sup> In addition to the ECJ's reasoning including that the national court in its order of reference found that Mr Derouin fell within the personal scope of the Regulation, Advocate General Mengozzi stated that it was clear from the documents before the ECJ that Mr Derouin sought to benefit from Art. 14 of the Treaty (independent professional services). This article provides, in essence, that the United Kingdom has the authority to tax the income that is attributable to a fixed base, which a French resident has regularly available to him in the United Kingdom for the purpose of performing work in an independent capacity. In this respect, it should be noted that Art. 14 of the OECD Model Convention (hereinafter: the OECD Model) was deleted as of 2000.<sup>32</sup> Income from independent personal services was integrated into Art. 7 of the OECD Model (business profits). Many tax treaties, however, still contain a provision similar to Art. 14 of the OECD Model, such as the Treaty.

The wording of Art. 14 of the Treaty, as such, does not require that Mr Derouin personally perform activities in the United Kingdom, whilst residing in France.<sup>33</sup> This approach is also adopted by the OECD.<sup>34</sup> As a result, the former Art. 14 of the OECD Model also applies to income derived by a person from services he performed through a fixed base in the source state even though he does not, in fact, provide services in that state.<sup>35</sup> Art. 14 of the Treaty assigns the taxation right to the United Kingdom if and insofar as Mr Derouin has a fixed base regularly available to him in the United Kingdom for the purpose of performing the activities. There is some debate<sup>36</sup> as to whether or not income derived from services performed by international law firms operating in numerous countries can be classified under the previous Art. 14 of the OECD Model.<sup>37</sup> It could be argued that the various partners of the firm are taxable in the different states in which the firm has offices, at least if the partnership is considered to be transparent for tax purposes from the perspective of the states concerned.<sup>38</sup> This also appeared to be the case for Mr Derouin who was a partner of an international law firm, *i.e.* Linklaters, which was governed by English law with its head office in the United Kingdom and offices in other Member States, including France.<sup>39</sup> The London office of Linklaters constituted a

fixed base for Mr Derouin and his part of the profits attributed to the fixed base was taxable in the United Kingdom under Art. 14 of the Treaty.<sup>40</sup>

The Advocate General appeared to read in the application of Art. 14(1) of the Treaty that Mr Derouin worked in a self-employed capacity in the United Kingdom, which was, according to the Advocate General, also supported by the fact that Mr Derouin was registered with the Supreme Court of England and Wales as a foreign

30. France intervened in the preliminary proceedings before the ECJ. It is striking that France subscribed to Mr Derouin's arguments, thereby contradicting Urssaf's reasoning.

31. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Paras. 36 and 37.

32. This deletion was a consequence of the OECD Report entitled "Issues Related to Article 14 of the OECD Model Tax Convention", Issues in International Taxation, No. 7 (Paris: OECD, 2000). The Report is discussed by J.W.J. de Kort, "Why Article 14 (independent personal services) was deleted from the OECD Model Tax Convention", *Intertax* (2001), Vol. 29, No. 3, p. 74 et seq.

33. The US Internal Revenue Service (IRS) in Rev. Rul. 2004-3 explicitly confirmed that a German resident partner of a German service partnership (a law firm) with a fixed base in the United States is deemed to provide his services personally in the United States and to have a fixed base available to him in the United States, even though he does not in fact perform any services in the United States. According to the IRS, this also applies to other tax treaties containing a provision that is similar to Art. 14 of the 1989 Germany—US tax treaty. See also R. Goulder, "Treasury clarifies application of tax treaties to foreign service partnership", *Tax Notes International*, 9 February 2004, p. 510 and G. May, "Wrongs and Remedies in the U.S. tax treatment of multinational partnerships of individuals", *Tax Notes International*, 2 August 2004, p. 447.

34. Compare the OECD Report, note 32, Paras. 18 and 44.

35. See explicitly with regard to the application of Art. 14 of the OECD Model to partnerships, the OECD Report, note 32, Para. 44. See also M. Van Keirsblick, "Artikel 14 – Zelfstandige beroepen", B. Peeters (ed.) *Het Belgisch–Nederlands dubbelbelastingverdrag* (Ghent: Larcier, 2008), p. 373. A different view, *i.e.* the application of Art. 14 of the OECD Model requires the personal performance of activities by the partner in the source state, is shared by D. Endres and H. Debatin, "Taxation of International Law Firms in Germany", *Tax Planning International Review* (1996), No. 1, pp. 8–10 and A. Hemmelrath, "Art. 14 – Selbständige Arbeit", in K. Vogel and R. Lehner, *Doppelbesteuerungsabkommen* (Munich: Verlag C.H. Beck, 2008), pp. 1157 and 1158. This is also noted by the OECD in its Report, note 32, Para. 18 et seq. The OECD, however, opted for another approach.

36. C. van Raad, *Cursus Belastingrecht (Internationaal Belastingrecht)* (Deventer: Kluwer, loose-leaf), Para. 3.4.5.A.

37. The former Art. 14(2) of the OECD Model noted the independent activities of lawyers as one of the examples of the term "professional services" falling within the meaning of the previous Art. 14(1).

38. This view is also shared by the OECD in its Report, note 32, Para. 44. ("According to the Committee, when applying Article 14 to the income allocated to each partner, the activities of the partnership must be attributed to the partners to the same extent as is the fixed base of the partnership, so that it may be said that each partner has a fixed base ... for the purpose of performing his activities.")

39. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 12, first dash.

40. Certain case law takes the view that Art. 7 of the OECD Model (business profits) applies to internationally operating law firms. Compare the decision of the Netherlands Supreme Court of 8 February 2002, BNB 2002/209 in which the Court was of the opinion that Art. 7 of the previous 1970 Belgium—Netherlands tax treaty applied to the profits derived by a Netherlands-based law firm maintaining a permanent establishment in Belgium rather than Art. 14 of that tax treaty (independent personal services). See also the Indian Income Tax Appellate of Mumbai in its decision of 27 September 2001 in *Cliff Chance (UK) v. Deputy Commissioner of Income Tax Chatuverdi VP, International Tax Law Reports*, 2002, p. 711, which explicitly considered that Art. 7 can apply to an internationally operating law firm. A similar approach is adopted by the South African Bloemfontein Tax Court in its decision of 8 May 2007, No. 12158 regarding the 1995 Lesotho—South Africa tax treaty (*IBFD Tax Treaty Case Law* (Internet), W.F.G. Wijnen (ed.)). See also R. Portner, "German perspective on Taxation of Multinational Law Firms with Cross-Border Organizations", *Tax Notes International* (2002), pp. 1301–1307.

lawyer.<sup>41</sup> In the authors' view, the fact that Mr Derouin was registered with the Supreme Court of England and Wales as a foreign lawyer does not automatically mean that he performed self-employed services in the United Kingdom.<sup>42</sup> The same can be said for Art. 14 of the Treaty applying to Mr Derouin's situation. Consequently, it is possible to agree with the ECJ's approach by not adopting the Advocate General's reasoning with regard to Art. 14 of the Treaty. Nevertheless, it is still unsatisfactory that the national court did not pay sufficient attention to Mr Derouin's statement that he did not perform any activities in a self-employed capacity in the United Kingdom. This is even more so, as the ECJ explicitly commented in its factual determination that Mr Derouin performed all his work as a lawyer for the Paris office of Linklaters, which could imply that he similarly provided his services entirely in France.<sup>43</sup>

The ECJ concluded that Mr Derouin fell under Art. 14a(2) of the Regulation.<sup>44</sup> This article provides that a person who is normally self-employed in the territory of two or more Member states (France and the United Kingdom) are subject to the legislation of the Member State in whose territory he resides (France) if he pursues any part of his activity in the territory of that Member State (France). The ECJ, therefore, concluded that Mr Derouin was exclusively subject to French legislation in accordance with this provision.<sup>45</sup>

#### 4. Ratione Materiae of the Regulation and the Treaty

A peculiarity of *Derouin* is that the CSG and CRDS fall within the scope of both the Treaty and the Regulation, as they meet the criteria of "tax" under the Treaty<sup>46</sup> and "social security legislation" under the Regulation.<sup>47</sup> In general, social security contributions are not covered by a tax treaty. This is confirmed by the Commentary on Art. 2 of the OECD Model, i.e.:

Social security charges, or any other charges paid where there is a direct connection between the levy and the individual benefits to be received, shall not be regarded as "taxes on the total amount of wages."<sup>48</sup>

The ECJ, however, commented that the CSG and CRDS lack a direct connection with the individual benefits to be received. In principle, all residents of France paying income taxes are subject to the CSG and CRDS, in which context their occupational status or the nature of the social security system of which they formed part is irrelevant. Residence for tax purposes is the only relevant criterion to be liable to the CSG and CRDS. The ECJ also noted that an important feature of the payment of the CSG and CRDS is that it did not give the payer the right to claim social security benefits. As a result, the contributions should be regarded as tax within the meaning of Art. 1(2) of the Treaty. In addition, the ECJ referred to the 2004 France–UK tax treaty,<sup>49</sup> which explicitly referred to the CSG and CRDS as "[t]axes which are the subject of [the tax treaty]."<sup>50</sup>

Nevertheless, the ECJ in two decisions pre-dating *Derouin* has characterized the CSG and CRDS as being part of the French social security legislation within the meaning of the Regulation. Consequently, these contributions fall within the scope of the Regulation. The Commission also started infringement proceedings against France, as France imposed the CSG and CRDS on wages of all residents of France, i.e. also on those residents who worked exclusively outside France. Under Art. 13(2)(a) and (b) of the Regulation, however, the French social security legislation is not designated to apply to residents of France performing their activities exclusively in another Member State. The main question in these decisions was whether or not the CSG and CRDS fell within the scope of the Regulation. France argued in the infringement proceedings that the CSG and CRDS constituted taxes according to French national law,<sup>51</sup> rather than social security charges, even though the CSG was included in the French Social Security Code (*Code de la sécurité sociale*, CSS) and the CRDS was introduced by an order explicitly referring to the CSS.<sup>52</sup> Furthermore, the 2004 France–UK tax treaty also explicitly regarded the CSG and CRDS as income taxes falling within its scope.<sup>53</sup> The

41. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 38. This is also noted in ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 12, second dash.

42. The registration could be explained by the fact that he was a partner of an originally UK-based law firm in which connection the English legislation required all partners to be registered in England.

43. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 12.

44. *Id.*, Para. 21.

45. *Id.*

46. Art. 1 Treaty

47. Art. 1(j) in conjunction with Art. 4 Regulation.

48. Para. 3, last sentence of the Commentary to Art. 2(2) of the OECD Model. See also A.J. Martín Jiménez, "Defining the Objective Scope of Income Tax Treaties: The Impact of Other Treaties and EC Law on the Concept of Tax in the OECD Model", *Bulletin for International Fiscal Documentation*, 10 (2005), pp. 432-444.

49. The 2004 France–UK tax treaty did not apply to Mr Derouin, as it never entered into force. In this respect, France and the United Kingdom signed a new tax treaty on 19 June 2008 which is intended to replace the Treaty. The 2008 France–UK tax treaty also contained an explicit mention of the CSG and CRDS as taxes within the meaning of the treaty (Art. 2(1)(b)(v) and (vi)).

50. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 11.

51. The French Constitutional Court (*Conseil Constitutionnel*) had already ruled in a decision of 28 December 1990 that the CSG had to be characterized as a tax, *Journal officiel de la République française*, 30 December 1990, p. 16609. See also *Revue de jurisprudence fiscale* (1991), p. 127 and L. Philip, "La décision du 29 décembre 1990 du Conseil constitutionnel sur la contribution sociale généralisée et la notion d'impôt", *Droit fiscal* (1991), p. 612.

52. ECJ, 15 February 2000, Case C-34/98, *Commission of the European Communities v. French Republic*, on the CRDS, Paras. 33 and 34 and ECJ, 15 February 2000, Case C-169/98, *Commission of the European Communities v. French Republic*, on the CSG, Paras. 31 and 32.

53. It can be assumed that France and the United Kingdom in 2004 were aware of the ECJ's approach in its decisions of 2000, meaning that the Regulation encompassed these charges. Nevertheless, France and the United Kingdom explicitly and deliberately opted to include these charges in the 2004 France–UK tax treaty. The same applies, mutatis mutandis, to the 2008 France–UK tax treaty.

ECJ, however, held that the CSG and CRDS should be regarded as social security charges for purposes of the Regulation. Instead of following a definition similar to that in the Commentary on the OECD Model, the ECJ held:

that there must be a link between the provision in question and the legislation governing the branches of social security listed in Art. 4 of Regulation No. 1408/71, and that that link must be direct and sufficiently relevant.<sup>54</sup>

The ECJ concluded that a direct and sufficiently relevant link was present, as the proceeds from the CSG and CRDS were used to finance the social security benefits that are covered by Art. 4(1) of the Regulation.<sup>55</sup> This conclusion was not altered by the fact that the CSG and CRDS did “not give entitlement to any direct and identifiable benefit in return.” Had such an entitlement existed, the ECJ’s conclusion would have been in accordance with the definition given by the Commentary on the OECD Model.<sup>56</sup> *Derouin* demonstrates that a levy can simultaneously fall within the material scope of the Regulation and the Treaty, as the definitions in the Regulation and the Treaty may differ.

According to the definition of social security charges provided by the ECJ, a direct and sufficient connection must be established between the levy in question and the “the branches of social security” listed in Art. 4 of the Regulation. For this reason, the ECJ sought to establish a link other than with the Treaty. In this respect, the Treaty emphasizes the connection between the payer of the premiums and the right to claim social security benefits. The ECJ held that establishing a more indirect link between the charges and the social security legislation was relevant. Consequently, the ECJ adopted an approach under which the relevant connection did not have to exist at the level of the individual premium payer, who had the right to claim benefits. In the ECJ’s view, the connection must be made at a legislative level, i.e. the proceeds derived from the charges must be employed to finance the social security benefits. Even though the ECJ regarded this link as direct, it is less direct than the Treaty accepts.

In the authors’ opinion, the rationale behind the approach adopted by the ECJ is the definition of social security legislation in Art. 1(j) of the Regulation, which states that:

legislation means in respect of each Member State statutes, regulations and other provisions and all other implementing measures, present or future, relating to the branches and schemes of social security covered by Article 4 (1) and (2) or those special non-contributory benefits covered by Article 4 (2a). (emphasis added)

The wording of Art. 1(j) of the Regulation requires a relationship between “regulations and other provisions and all other implementing measures”, including charges and “branches and schemes of social security”.

It should be noted that the ECJ’s reasoning entailing the establishment of a connection between the charges and the purpose for which the proceeds from these charges are used is not entirely new. It resembles the ECJ’s

approach with regard to parafiscal taxes relating to State aid. Such aid is illegal when it is not notified to and approved by the Commission. Art. 88(3) of the EC Treaty imposes a standstill obligation on Member States in respect of illegal State aid, requiring that *all implementing measures* are postponed. A parafiscal tax financing the illegal State aid can be characterized as an implementing measure regarding the aid. Such measures cannot be levied and must possibly be repaid. Specifically, the ECJ held in *Streekgewest*<sup>57</sup> that:

[f]or a tax, or part of a tax, to be regarded as forming an integral part of an aid measure, it must be hypothecated to the aid measure under the relevant national rules, in the sense that the revenue from the tax is necessarily allocated for the financing of the aid. In the event of such hypothecation, the revenue from the tax has a direct impact on the amount of the aid and, consequently, on the assessment of the compatibility of the aid with the common market.<sup>58</sup>

The ECJ is of the opinion that parafiscal taxes should be regarded as *implementing measures* of State aid when their revenues are destined to finance this aid. This is, at least to a certain extent, comparable to the CSG and CRDS, which could be regarded as *implementing measures* financing social security benefits in this respect.

Even though the ECJ’s approach establishing a link with regard to the CSG and CRDS between the charges and the social security legislation is based on the language of Art. 1(j) of the Regulation and although the ECJ adopted a comparable reasoning in established case law regarding State aid, the authors are of the opinion that it is not an appropriate criterion to determine the connections in *all cases*. Taking the view that the connection with the individual benefiting from the social security is unimportant may result in situations in which indirect taxes could also be characterized as social security levies, provided that the resulting revenue was hypothecated to social security benefits, for example, the proceeds from sales or waste taxes that are allocated to finance social security benefits. This would be a striking result, thereby making it difficult or even impossible to apply the conflict rules of the Regulation, as these take an individual performing services as the point of attachment. An individual, for instance, could refuse to pay a sales tax in a Member State in which the revenue is destined to finance a social security benefit, as its social security legislation is not designated by the Regulation to apply.

54. ECJ, 15 February 2000, Case C-34/98, *Commission of the European Communities v. French Republic*, on the CRDS, Paras. 35 and 34 and ECJ, 15 February 2000, Case C-169/98, *Commission of the European Communities v. French Republic*, on the CSG, Para. 33.

55. Id., Case C-34/98, CRDS, Para. 37 and Id., Case C-169/98, CSG, Para. 35.

56. Id., Case C-34/98, CRDS, Para. 39 and Id., Case C-169/98, CSG, Para. 37.

57. ECJ, 13 January 2005, Case C-174/02, *Streekgewest Westelijk Noord-Brabant v. Staatssecretaris van Financiën*. The case concerned State aid in the form of an exemption from Netherlands waste tax for both de-inking residues and waste from the recycling of plastic materials. The rate of waste tax was increased by NLG 0.70 (EUR 0.32) per ton of waste when the exemption was introduced. *Streekgewest* refused to pay the increase, as it considered the increase to be an implementing measure regarding State aid. According to the ECJ, the link between the levy and the State aid was, however, insufficient.

58. Id., Para. 26.

Consequently, the authors are of the opinion that the ECJ's approach is only effective in the case of direct taxes levied from individuals ultimately benefiting from the social security system if a link with the right to claim the benefits is also absent at the individual's level.

## 5. Simultaneous Application of the Regulation and the Treaty

The Regulation distinguishes between national social security legislation<sup>59</sup> and social security conventions.<sup>60</sup> The ECJ in *Grana-Novoa*<sup>61</sup> confirmed this distinction, i.e.:

the concept of "legislation" referred to in [Art. 1(j) of the Regulation] does not cover the provisions of international social security conventions concluded between a single Member State and a non-member State. That interpretation is not invalidated by the fact that such conventions have been incorporated as statute law into the domestic legal order of the Member State concerned.<sup>62</sup>

This distinction is important, as, on the one hand, the Regulation coordinates the application of national social security legislations by providing conflict rules, whilst, on the other, it replaces exclusively social security conventions between Member States on its entry into force.<sup>63,64</sup> Some exceptions are, however, permitted to the last rule. One of the major exceptions is Art. 7(2)c of the Regulation. This states that the Regulation does not affect obligations arising from:

certain provisions of social security conventions entered into by the Member States before the date of application of this Regulation provided that they are more favourable to the beneficiaries ...<sup>65</sup>

The question arises as to how the Treaty should be classified under the Regulation. In this respect, the following classifications are possible: (1) national social security legislation allowing the application of the Treaty, (2) social security convention, in which case the application of the Treaty would, in principle, be excluded and (3) both classifications under (1) and (2) do not apply, meaning that the Treaty would not fall within the scope of the Regulation, and disallowing its application.

The parties involved in *Derouin* all argued that the Treaty fell within the substantive scope of the Regulation. According to the Commission and Urssaf, the Treaty had to be characterized as a social security convention. Mr Derouin and France took the view that the Treaty constituted the exercise of powers within the meaning of the Regulation, as the Treaty had to be regarded as "legislation laid down in accordance with these provisions".<sup>66</sup> They were of the opinion that this expression included in Art. 14(d)(1) of the Regulation referred to all legislation of the Member State whose social security legislation is designated and encompassing the Treaty.

The Advocate General's Opinion in *Derouin* replied to Mr Derouin's argument, including that the Treaty should be regarded as national security legislation, as follows:

[t]his argument fails to convince, for it loses sight of the fact that Regulation No. 1408/71 merely designates the social security legislation applicable to employed and self-employed persons within the European Community who are in a given transborder situa-

tion and *does not therefore refer* to national legislation as a whole, which includes inter alia national employment law and *tax laws*. Under Article 14d(1) of Regulation No. 1408/71, and as the [Urssaf] considered, the designated social security legislation implementing that provision must base the assessment of contributions falling within the scope of that regulation on the total income from self-employment by a person in the situation covered by Article 14a(2) of that regulation. (emphasis added)<sup>67</sup>

The Advocate General opined that national tax law does not fall within the scope of the Regulation, as this primarily designates the application of social security legislation. A fortiori the Treaty could not be regarded as national security legislation. In the authors' opinion, the Advocate General denies the special features of the CSG and CRDS. Specifically, the CSG and CRDS are characterized as taxes under national law (at least in France's argument) and under the Treaty, whereas the ECJ held that these contributions were also covered by the Regulation. Consequently, the authors do not endorse the Advocate General's arguments.

The Advocate General also adhered to the Commission's statement that the Treaty should be treated as a social security convention under the Regulation. In this respect, he stated:

However, as the [Urssaf] and the Commission have aptly pointed out, social security conventions concluded between two or more Member States and the provisions of any convention which, regardless of the fact that it does not formally govern the area of social security, falls within the scope of Regulation No. 1408/71, form the subject of specific provisions of that regulation, that is to say, Articles 6 to 8 thereof.

We are aware that Article 6 of Regulation No. 1408/71 sets out the principle that that regulation replaces inter alia any social security convention binding two Member States exclusively. That principle should, in my view, extend to the provisions of

59. Art. 1(j) Regulation.

60. Art. 6 et seq. Regulation.

61. ECJ, 2 August 1993, Case C-23/92, *Maria Grana-Novoa v. Landesversicherungsanstalt Hessen*.

62. Id., Para. 29.

63. According to Art. 99 of the original Regulation (OJ 1971, L 149 /2), it entered into force "on the first day of the seventh month following the publication in the Official Journal of the European Communities of the implementing Regulation", Regulation (EEC) No. 574/72 of the Council of 21 March 1972 determining the procedure for implementing Regulation (EEC) No. 1408/71 on the application of social security schemes to employed persons and their families moving within the Community was published on 27 March 1972 (OJ 1972, L 74/1). As a result, the Regulation entered into force on 1 October 1972 (Art. 6(a)). The Implementing Regulation entered into force on the same day (Art. 122).

64. Subject to Art. 7, Art. 8 and Art. 46(4) Regulation.

65. This provision codifies established case law of the ECJ on the principle of the most favourable treatment. See ECJ, 7 February 1991, Case C-227/89, *Ludwig Rönfeldt v. Bundesversicherungsanstalt für Angestellte*; ECJ, 9 November 1995, Case C-475/93, *Jean-Louis Thévenon and Stadt Speyer – Sozialamt v. Landesversicherungsanstalt Rheinland-Pfalz*; ECJ, 9 November 2000, Case C-75/99, *Edmund Thelen v. Bundesanstalt für Arbeit*; and ECJ, 5 February 2002, Case C-277/99, *Doris Kaske v. Landesgeschäftsstelle des Arbeitsmarktservice Wien*. It was introduced by Art. 1(3) of Regulation (EC) No. 647/2005 of the European Parliament and of the Council of 13 April 2005 amending Council Regulations (EEC) No. 1408/71 on the application of social security schemes to employed persons, to self-employed persons and to members of their families moving within the Community and (EEC) No. 574/72 containing the procedure for implementing Regulation (EEC) No. 1408/71 (OJ 2005, L 117/1).

66. Art. 14d(1) Regulation.

67. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, Para. 66.

other bilateral conventions which fall within the scope of that regulation. Any other interpretation would enable Member States to evade the principle laid down in Article 6 by allowing them, by merely using a classification procedure, to remove from the scope of that regulation provisions of a convention which fall within it.<sup>68</sup>

Whether or not the Treaty can be classified as a social security convention within the meaning of Art. 6 et seq. of the Regulation depends on the explanation given to the expression "social security convention". It is not under discussion that the Treaty covers the CSG and CRDS, which are also classified as social security contributions under the Regulation. Questions do, however, arise as to whether it suffices that a social security contribution is governed by the substantive scope of a tax treaty to characterize that tax treaty as a social security convention or whether the classification as a social security convention requires the fulfilment of other criteria.

The authors believe that the essential difference between taxation and social security is that social security legislation provides directly identifiable benefits to individuals. This would also influence the functioning of social security conventions with regard to tax treaties. In general, social security conventions are based on the following principles: (1) equal treatment, (2) exclusivity or unity of the applicable legislation, (3) the maintenance of acquired rights and the fulfilment of certain prescribed periods and (4) the export of benefits.<sup>69</sup> According to Suchy,<sup>70</sup> a tax treaty and social security convention, and, of course, the Regulation, differ regarding the following elements: (1) conflict,<sup>71</sup> (2) conflict rules,<sup>72</sup> (3) coordination methods<sup>73</sup> and (4) financial circuits arising from social security conventions.<sup>74</sup>

In the authors' opinion, the Treaty cannot be characterized as a social security convention, as it (1) only concerns the levying of taxes, (2) does not directly provide benefits to individuals derived from funds to which the Treaty may apply and (3) lacks the other elements of a social security convention noted previously. Consequently, the Treaty cannot be governed by the scope of Art. 6 et seq. of the Regulation.

In contrast to the Advocate General's Opinion, the ECJ in *Derouin* did not devote explicit attention to the various features of classifying or non-classifying the Treaty under the Regulation. Nevertheless, the ECJ endorsed the analysis of Mr Derouin and France, as it considered that the Treaty is part of:

the determination of the tax base for social contributions ..., in the absence of harmonisation at Community level, it is for the legislation of the Member State concerned to determine the income to be taken into account when calculating those contributions. (emphasis added)<sup>75</sup>

Subsequently, the ECJ stated that:

the exclusion of the foreign source income from the tax base for social contributions concerned results from the provisions of the applicable national law (emphasis added).<sup>76</sup>

Consequently, the ECJ characterized the Treaty as national legislation. This may be supported by the CSG and CRDS having a hybrid character in this respect. The

ECJ also held that the CSG and CRDS fell under the Treaty. The tax base for purposes of the CSG and CRDS would exclude Mr Derouin's UK-source income when the rules of the Treaty are followed. Despite the fact that applying the provisions of the Treaty would result in a smaller tax base when calculating the CSG and CRDS, Art. 1(j) of the Regulation would continue to encompass the CSG and CRDS. Accordingly, it appears to be arguable that the Treaty, in combination with the CSG and CRDS, falls within the scope of Art. 1(j) of the Regulation.

## 6. Single State Principle and Principle of Overriding Effect

### 6.1. In General

One of the major objectives of the Regulation is the single state principle, i.e. the authority to levy social security contributions is assigned to only one Member State to the exclusion of the other Member State's social security legislation. This is confirmed by the Preamble to the Regulation.<sup>77</sup> The doctrine of the single state principle has been developed by the ECJ in *Ten Holder*,<sup>78</sup> *Luijten*<sup>79</sup>

68. Id., Paras. 69 and 70.

69. E. Traversa and M. Paolillo, "Convergences et divergences entre le droit fiscal et le droit de la sécurité sociale à la lumière du contexte communautaire et international", *Revue générale de fiscalité*, No. 1, Vol. 38 (2008), pp. 23-36.

70. G.R. Suchy, "National Report France", in (ed.) M. Lang, "Double Taxation Conventions and Social Security Conventions", *Internationales Steuerrecht*, No. 43 (2006), pp. 259-315, especially pp. 280-285. See also F. Pennings and M. Weerepas, "Towards a convergence of coordination in social security and tax law?", *EC Tax Review*, No. 4, Vol. 15 (2006), pp. 215-225.

71. According to Suchy, note 70, tax treaties, generally, intend to resolve positive conflicts, i.e. two states apply their domestic tax laws to the same item of income. In Suchy's view, social security conventions attempt to provide a solution for negative conflicts, i.e. endeavour to prevent the non-application of domestic social legislations when cross-border activities are performed.

72. Tax treaties divide taxation rights and provide elimination of double taxation and contain exclusive and shared taxation rights. With regard to a shared taxation right, both the source and residence state have a taxation right in which connection the residence state must eliminate double taxation for the income that may be taxed in the source state. Social security conventions normally contain the single state principle.

73. The avoidance of double taxation by granting an exemption or providing a tax credit. Social security conventions normally provide exclusivity, in addition to the exportability of social security benefits and taking account of insured periods spent in foreign countries.

74. Social security benefits may be exported. This means that an individual may still claim benefits from his former residence state following emigration. Social security conventions often state that the individual is entitled to claim the exported social security benefits from authorities in his new residence state. This is not altered by the fact that social security contributions were previously paid to the authorities in the individual's former residence state. As a result, the authorities of the former residence state transfer funds to the authorities of the new residence state to compensate the latter state for granting the social security benefits to the individual. Consequently, financial ties may exist between these authorities. Tax authorities of different states, generally, do not levy taxes on behalf of authorities of another state. An exception is the revenue sharing that is included in Protocol II accompanying the 2001 Belgium-Netherlands tax treaty regarding income from employment and the revenue sharing in Art. 12(1) of Council Directive 2003/48/EC of 3 June 2003 on taxation of savings income (OJ 2003, L 157/38).

75. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et allocations familiales de Paris - Région parisienne (Urssaf de Paris - Région parisienne)*, Para. 24.

76. Id., Para. 30.

77. Eighth recital Preamble.

78. ECJ, 12 June 1986, Case 302/84, A.A. *Ten Holder v. Bestuur van de Nieuwe Algemene Bedrijfsvereniging*.

79. ECJ, 10 July 1986, Case 60/85, M.E.S. *Luijten v. Raad van Arbeid*.

and *Kits van Heijningen*.<sup>80</sup> It should be noted that a number of exceptions to the single state principle are permitted, for example, Art. 14c(b) of the Regulation.<sup>81</sup>

In addition to the single state principle, some scholars also recognize the principle of overriding effect underlying the Regulation.<sup>82</sup> According to Cornelissen, the single state principle and the principle of overriding effect are the mirror image of each other,<sup>83</sup> i.e. they are mutually supplementary. When the Regulation based on the single state principle designates a Member State's social security legislation to exclusively apply, the principle of overriding effect ensures that the designated national social security legislation cannot exclude the individual concerned from the territorial application of that national security legislation, otherwise, the migrant individual would have been deprived of social security protection, which contradicts the primary objective of the Regulation.<sup>84</sup> In the authors' view, the principle of overriding effect guarantees the effectiveness of the Regulation. When the social security legislation of a Member State is exclusively designated by virtue of the Regulation, the consequence of the principle of overriding effect is that the domestic legislation of that Member State cannot impede or avoid the effective obligation to grant social security benefits based on a residence requirement. Schoukens describes this strikingly as "the designated country has to cover the concerned person, even if according to its own territorial scope of application this would not be the case."<sup>85</sup>

The principle of overriding effect does not affect the material scope of social security benefits or social security contributions, as it only involves the territorial scope. The principle of overriding effect is incapable of creating rights to social security benefits that did not exist under the national social security legislation of the competent Member State. This principle also cannot create obligations to pay social security contributions that the national social security legislation of the Member State concerned did not provide for.

To the authors' knowledge, the ECJ's decisions did not explicitly recognize the principle of overriding effect, even when the ECJ was explicitly challenged to state and apply this principle, for example, in *Ten Holder*.<sup>86</sup> The ECJ also did not confirm, but it did not deny, that the Regulation is based on the principle of overriding effect. Kavelaars is of the opinion that the ECJ in its judgments in *Daalmeijer*<sup>87</sup> and *Zinnecker*<sup>88</sup> recognized the principle of overriding effect.<sup>89</sup>

The non-discrimination principle is another angle from which the obligation for the designated Member State to deny residence requirements can be considered, especially regarding the free movement of employees<sup>90</sup> and self-employed workers.<sup>91</sup> These provisions also prohibit the indirect discrimination of these types of workers by applying residence requirements.<sup>92</sup> Accordingly, the principle of non-discrimination and the principle of overriding effect have the same result, i.e. the residence requirements of the designated social security legislation do not apply.

If it is accepted that the principle of overriding effect underlies the Regulation, the question can be raised as to whether the principle would apply to both social security benefits and social security contributions or whether it would only apply to benefits and not contributions. *Derouin* appears to cast some light on the last aspect (see 6.2. and 6.3.).

## 6.2. *Derouin* differs from *Allard*

Given these principles, Urssaf, the United Kingdom and the Commission argued in the proceedings before the ECJ that the Member State whose social security legislation is designated by the Regulation must include all income in the tax base for social contributions. They made reference to the ECJ's judgment in *Allard*,<sup>93</sup> as they

80. ECJ, 3 May 1990, Case C-2/89, *Bestuur van de Sociale Verzekeringsbank v. M.G.J. Kits van Heijningen*.

81. Art. 14(c) of the Regulation contains special rules for persons who are simultaneously employed in the territory of one Member state and self-employed in the territory of another Member State. This provision refers to some cases mentioned in Annex VII to the Regulation. This Annex refers to instances in which a person is subject simultaneously to the legislation of two Member States, for example, if a person is self-employed in one Member State and gainfully employed in another Member State. In situations falling under Annex VII, the obligation to pay social security contributions is divided between two Member States, i.e. the person in question has to pay social security contributions in the Member States in which he provides professional services. This entails that he is, in principle, also entitled to social security allowances in both states. In this respect, see the ECJ's decision in *de Jaeck*. The Court in ECJ, 20 May 2008, Case C-352/06, *Brigitte Bosmann v. Bundesagentur für Arbeit – Familienkasse Aachen*, Para. 32 also stated that the single state principle "cannot serve as a basis for precluding a Member State, which is not the competent State but which does not subject the right to child benefit to conditions of employment or insurance, from being able to grant such a benefit to one of its residents, since the possibility of such a grant arises, in actual fact, from its legislation".

82. R. Cornelissen, "Communautaire en Nederlandse jurisprudentie inzake de conflictrechtsregels in het Europees en internationaal sociaal zekerheidsrecht", *Tijdschrift voor Europees en economisch recht* (1986), pp. 799-823; P. Kavelaars, *Toewijzingsregels in het internationaal fiscaal en sociaalverzekeringsrecht* (Deventer: Kluwer, 2003), p. 134; and P.S.J.M. Schoukens, "Introduction to social security co-ordination in the EU", *Izbanregren Broi Nationalen Oseguriten Institut* (2005).

83. Cornelissen, note 82, p. 801.

84. ECJ, 9 November 2006, Case C-205/05, *Fabien Nemeč v. Caisse régionale d'assurance maladie du Nord-Est*, Paras. 37 and 38 and the case law referred to in these paragraphs.

85. Schoukens, note 82, p. 25.

86. ECJ, 12 June 1986, Case 302/84, *A.A. Ten Holder v. Bestuur van de Nieuwe Algemene Bedrijfsvereniging*, Para. 17.

87. ECJ, 21 February 1991, Case 245/88, *HCM Daalmeijer v. Bestuur van de Sociale Verzekeringsbank*, Para. 14.

88. ECJ, 13 October 1993, Case C-121/92, *Staatssecretaris van Financiën v. A. Zinnecker*.

89. Kavelaars stated in 1992 that the ECJ in *Daalmeijer* only implicitly referred to the principle of overriding effect (*Toewijzingsregels in het internationaal fiscaal en sociaalverzekeringsrecht* (Deventer: Kluwer, 1992), p. 112). He concluded in 2003 (*Toewijzingsregels in het internationaal fiscaal en sociaalverzekeringsrecht* (Deventer: Kluwer, 2003), p. 135) that the ECJ in *Daalmeijer* explicitly pointed to the principle of overriding effect (confirmed in 2008 as co-author of A.C.G.A.C. de Graaf, P. Kavelaars and A.J.A. Stevens, *Internationaal Belastingrecht* (Deventer: Kluwer, 2008), p. 376). Kavelaars indicated in 1994 and in 1997 ("Ontwikkelingen aan het internationaal sociaal-verzekeringsfront", *Weekblad Fiscaal Recht* 1994/1052 and "Bewegelijkheid in het Europees sociaal verzekeringsrecht", *Weekblad Fiscaal Recht* 1997/1791) that the ECJ in *Zinnecker* had adopted the principle of overriding effect.

90. Art. 39 EC Treaty.

91. Art. 43 EC Treaty.

92. ECJ, 12 February 1974, Case 152/73, *Giovanni Maria Sotgiu v. Deutsche Bundespost* recognized this for the first time.

93. ECJ, 26 May 2005, Case C-249/04, *José Allard v. Institut national d'assurances sociales pour travailleurs indépendants (Inasti)*.

believed that *Allard* supported their arguments. *Allard* involved Mr Allard who was resident in Belgium and was in receipt of income from professional activities pursued in a self-employed capacity in Belgium and in France. Mr Allard contested Belgium's possibility to assess the "moderation contribution" on his entire income, including the income he received in France. The proceeds from the moderation contribution were used to finance the self-employed persons' old-age and survivor's pension scheme. The ECJ held that:

Furthermore, Article 14d(1) of Regulation No. 1408/71 specifies that the person referred to in Article 14a(2) of that regulation is to be treated as if he pursued all his professional activity or activities in the territory of the Member State concerned (see, by analogy, Case C-71/93 *Van Pouke* [1994] ECR I-1101, paragraph 24).

Consequently, a person in the situation described in the order for reference who is simultaneously self-employed in Belgium and in France must be subject, as a result of the latter activity, to the appropriate Belgian legislation under the same conditions as if he was self-employed in Belgium (see by analogy, *Van Pouke*, paragraph 25).

It follows that a social security contribution such as the moderation contribution payable in Belgium by Mr Allard must be calculated taking into account the income received in France.

The answer to the first question must therefore be that Article 13 et seq. of Regulation No. 1408/71 require a contribution such as the moderation contribution to be calculated in such a way as to include under the heading of occupational income the income obtained in the territory of a Member State other than the Member State whose social legislation is applicable even if, after paying that contribution, the self-employed person cannot claim any social security or other benefit at the expense of that State.

...  
It follows from the answer to the first question that the relevant provisions of Regulation No. 1408/71 require account to be taken of the income received in another Member State for the purpose of calculating the moderation contribution payable by self-employed persons who are in Mr Allard's situation. (emphasis added)<sup>94</sup>

The Advocate General's Opinion in *Derouin* confirmed the reading of *Allard* given by Urssaf, the United Kingdom and the Commission. The Advocate General's view was based on Art. 14(d)(1) of the Regulation, which provides that:

[t]he persons referred to in Article 14(2)<sup>[95]</sup> and (3),<sup>[96]</sup> Article 14a(2), (3) and (4)<sup>[97]</sup>, Article 14c(a)<sup>[98]</sup> and Article 14e shall be treated, for the purposes of application of the legislation laid down in accordance with these provisions, as if he pursued all his professional activity or activities in the territory of the Member State concerned. (emphasis added)

It could be argued that the Advocate General recognized the principle of overriding effect to similarly apply to social security contributions. The ECJ was, however, of the opinion that *Allard* differed from *Derouin*. According to the ECJ the facts of *Allard* were that Belgium (the residence Member State) chose to include all the income earned by Mr Allard both on its territory and on that of the other Member State (France) in the tax base for social security contributions. The Regulation did not preclude Belgium from calculating these contributions on the entire income. As a result and given this context, the ECJ held in *Allard* that the contributions must, indeed, be calculated on total income.<sup>99</sup> According to the ECJ, this conclusion did not apply to Mr Derouin, as the

exclusion of the foreign-source income from the tax base for social security contributions resulted from the national law provisions, i.e. the Treaty.<sup>100</sup>

The ECJ in *Derouin* held that it is for the Member State concerned to determine the income to be taken into account when calculating the social security contributions.<sup>101</sup> According to the ECJ, it is, however, essential that the Member State complies with EC law when it exercises this power.<sup>102</sup> The ECJ also held that this power of the Member States is not unlimited. The Member States are, in particular, required to respect the spirit and principles of the Regulation, including the single state principle, to ensure that a person is not penalized for exercising his right to free movement and to satisfy themselves that the system thereby created does not deprive that person of social protection.<sup>103</sup> Consequently, as EC law now stands, a Member State is entitled to forgo, unilaterally or in the context of a tax treaty, the inclusion in the tax base for social security contributions, such as the CSG and the CRDS, of income earned in the United Kingdom by Mr Derouin,<sup>104</sup> provided that the individual can still claim the social security benefits.<sup>105</sup> The Regulation does not interfere with the composition of the income on which social security contributions are determined. As a result, a Member State is free to take the total income as base in calculating social security contributions, for example Belgium in *Allard*, or to exclude a part of that income, for example France in *Derouin*, due to a tax treaty assigning the authority to tax that income to, in this case, the United Kingdom.

The authors agree with the ECJ's decision in *Derouin*, as it is based on the object and purpose of the Regulation, i.e. coordination. It also aligns with a system of coordination that Member States maintain their authority to establish the base for purposes of levying social security contributions.

94. Id., Paras. 21 to 24 and 27.

95. This provision contains special rules for persons, other than mariners, engaged in paid employment in which connection the person concerned is normally employed in the territory of two Member States.

96. This provision determines that the provisions of the legislation of a Member State for reduction, suspension or withdrawal of benefit in the case of a person in receipt of invalidity benefits or anticipatory old-age benefits pursuing a professional or trade activity may be invoked against such person even though he is pursuing his activity in the territory of another Member State.

97. Special rules for persons, other than mariners, who are self-employed.

98. Special rules for persons who are simultaneously employed in the territory of one Member State and self-employed in the territory of another Member State whose situation does not fall under Annex VII accompanying the Regulation.

99. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne* (Urssaf de Paris – Région parisienne), Para. 29.

100. Id., Para. 30.

101. Id., Para. 24. See also ECJ, 18 July 2006, Case C-50/05, *Maija T.I. Nikula*, Para. 24 and ECJ, 26 January 1999, Case C-18/95, *F.C. Terhoeve v. Inspecteur van de Belastingdienst Particulieren/Ondernemingen buitenland*, Para. 51.

102. Id. See also ECJ, 26 January 1999, Case C-18/95, *F.C. Terhoeve v. Inspecteur van de Belastingdienst Particulieren/Ondernemingen buitenland*, Para. 34 and ECJ, 7 July 2005, Case C-227/03, *A.J. van Pommeren-Bourgondiën v. Raad van bestuur van de Sociale verzekeringsbank*, Para. 39.

103. Id., Para. 25.

104. Id., Para. 27.

105. Id., Para. 31.

### 6.3. Can the competent Member State forgo levying social security contributions?

The question arises as to whether Member States can totally forgo the levying of social security contributions under their national legislation or a tax treaty, provided that the relevant individual continues to be entitled to social security benefits in the State whose legislation is designated by the Regulation. In this respect, the Netherlands Supreme Court's decision of 8 July 1997 (BNB 1997/310) is illustrative. According to the Netherlands Supreme Court, the principle of overriding effect is relevant to the entitlement to social security benefits and the obligation to pay social security contributions, but not to the actual levying of social security premiums pursuant to the domestic law. The Netherlands Supreme Court held that, if domestic law does not provide for possibilities to levy premiums, this cannot follow from the rules of international and EC law. Consequently, the obligation to pay social security contributions could only be effected if a domestic law explicitly provided for this possibility, even though the Regulation designated the Netherlands social security legislation to apply to a certain cross-border situation. In the absence of a domestic law base, an entitlement to social security benefits could exist without an obligation to pay social security contributions, as the domestic law did not provide for levying these contributions despite the fact that the Regulation designated Netherlands social security legislation to apply.<sup>106</sup>

To a certain extent, *Derouin* presents a comparable picture, as the base for calculating social security contributions does not comprise Mr Derouin's total income, but this element does not affect his entitlement to social security benefits. According to the authors, there is a certain connection between the decision of the Netherlands Supreme Court in BNB 1997/310 and the ECJ's decision in *Derouin*, provided that it is possible to regard BNB 1997/310 as a situation in which the Netherlands unilaterally chose not to levy social security contributions and despite the fact that the Netherlands social security legislation's application was designated by the Regulation. The ECJ confirmed in *Derouin* that, when the French social security legislation is designated by the Regulation, an obligation to pay social security contributions arises in France, in which context it would not be required that the French legislation would contain the possibility that these contributions were actually due. France is, however, under its national law not required to calculate these contributions on the total income, but it is, instead, permitted that a part of the income is excluded, for instance, because of the interrelationship with a tax treaty assigning the taxation right to another state.

The analysis of the ECJ in *Allard* demonstrates that the Regulation does not affect the way in which the competent Member State levies social security contributions. It is, however, questionable whether or not that Member State can also entirely forgo the levy of social security contributions. According to the ECJ in *Derouin*, the competent Member State is required:

to respect the spirit and the principles of Regulation No. 1408/71, including the single State principle applicable to social security, to ensure that a person is not penalised for exercising his right to free movement and to satisfy themselves that the system thus created does not deprive that person of social protection.<sup>107</sup>

In this respect, it is striking that the ECJ did not refer to the principle of overriding effect. Specifically, the ECJ only explicitly referred to the single state principle. This may imply that the principle of overriding effect does not underlie the Regulation. The ECJ also appeared to refer to the non-discrimination and free movement provisions, as it commented that the competent Member States are compelled to "ensure that a person is not penalised for exercising his right to free movement".<sup>108</sup> In addition, it should be noted that the ECJ emphasized the interest of social protection. According to the authors, this emphasis could mean that the ECJ only intended to point to social security *benefits* rather than to social security *contributions*. The authors are of the opinion that this is supported by the following statement of the ECJ in *Derouin*:

that the exclusion from the tax base for social security contributions of a worker's foreign source income cannot affect the worker's right to receive all of the benefits provided for by the applicable legislation.<sup>109</sup>

The ECJ clearly distinguished in this quotation between social security *benefits* and social security *contributions*, at least with regard to the competent Member State's obligations stemming from the Regulation. These Member States cannot deprive the individual of his right to receive social security benefits. A Member State is, however, free whether or not it levies social security contributions and in calculating these contributions. Consequently, assuming that the Regulation is, indeed, based on the principle of overriding effect, in the authors' view, this principle does not require the Member States to levy social security contributions and can even forgo, unilaterally or via a tax treaty, the levying of these contributions.

106. P. Kavelaars in his annotation accompanying the Netherlands Supreme Court's decision of 8 July 1997, BNB 1997/310, Para. 2 criticized this decision, as it would contravene the ECJ's decision in *Zinnecker*. The latter decision involved a resident of Germany who worked in a self-employed capacity in both the Netherlands and Germany. According to Kavelaars, the ECJ initially held that the principle of overriding effect of the Regulation meant that the individual concerned fell within the Netherlands social security system, but, finally, that the German social security legislation was designated to apply, as he also provided professional services in his residence state, Germany. Kavelaars also criticized the Netherlands Supreme Court for distinguishing with regard to the principle of overriding effect between social security *benefits* and social security *contributions*.

107. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 25.

108. In ECJ, 9 March 2006, Case C-493/04, *L.H. Piatowski v. Inspecteur van de Belastingdienst Grote Ondernemingen Eindhoven*, Paras. 19 and 20 and ECJ, 18 July 2006, Case C-50/05, *Maija T.I. Nikula*, Para. 20, the Court links the same wording ("... a person is not penalised ...") explicitly to the principle of equal treatment.

109. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 31.

## 7. Concurrence between the Regulation and Tax Treaties in Other Situations

The ECJ's judgment in *Derouin* is not limited to the cross-border activities of self-employed persons. A relationship between a tax treaty and the Regulation may arise in more cases, which is, inter alia, due to the fact that the conflict of law rules of the Regulation and the assigning rules of the tax treaties, generally, do not coincide. Without being complete, it is possible to establish that the respective rules may deviate regarding employment income (Art. 15 and Art. 16 of the OECD Model), business profits (Art. 7) and pension income (Art. 18).<sup>110</sup> In these cases, the tax treaty may allocate the taxation right on the income to the source state, whereas the Regulation designates the residence state's social security legislation to apply exclusively.

By virtue of *Derouin*, situations may arise in which total income is not taken into account in calculating the tax base for social security contributions, as the taxation right on the income is allocated to the source state under the relevant tax treaty and, consequently, the residence state must provide relief from double taxation. The authors believe that it does not make a difference whether the residence state provides relief through the credit or exemption method.

From the perspective of the Regulation, it is also irrelevant whether the UK partnership of whom Mr Derouin was a partner is regarded as transparent or opaque for tax purposes. The Regulation takes, as point of attachment, the individual and if he provides his services in which connection the characterization and the nature of his employer or the partnership through which he provides his services is unimportant. This is different for a tax treaty.

## 8. New Social Security Regulation No. 883/2004

The Advocate General's Opinion in *Derouin* referred to the new Social Security Regulation No. 883/2004<sup>111</sup> on several occasions. At the outset, he established<sup>112</sup> that the Regulation only applied to Mr Derouin's case rather than Regulation No. 883/2004. This new regulation will replace the Regulation once the Implementing Regulation<sup>113</sup> has entered into force.<sup>114</sup> Nevertheless, it is interesting to consider whether or not Derouin would be decided differently under this new Regulation. Art. 13(2) and (5) of Regulation No. 883/2004 are the essential provisions for situations similar to those of Mr Derouin and read as follows:

2. A person who normally pursues an activity as a self-employed person in two or more Member States shall be subject to:
  - (a) the legislation of the Member State of residence if he/she pursues a substantial part of his/her activity in that Member State;
  - ...
5. Persons referred to in paragraphs 1 to 4 shall be treated, for the purposes of the legislation determined in accordance with these provisions, as though they were pursuing all their activities as employed or self-employed persons *and were receiving all their income in the Member State concerned.* (emphasis added)

The last part of Para. 5 ("and were receiving all their income in the Member State concerned") was not included in the Commission's original proposal of Regulation No. 883/2004.<sup>115</sup> This phrase was added by the Council.<sup>116</sup> The Regulation also does not contain this type of addition. Specifically, Art. 14d(1) of the Regulation states that:

[t]he person referred to in Article 14(2) and (3), Article 14a(2), (3) and (4), Article 14c(a) and Article 14e shall be treated, for the purposes of application of the legislation laid down in accordance with these provisions, as if he pursued all his professional activity or activities in the territory of the Member State concerned.

The Commission's original proposal did not intend to substantially change this provision.<sup>117</sup> Apparently, the addition was made on the request of Spain, when discussing this provision during a meeting of the Working Party on Social Questions of the Council of the European Union, i.e.:

Spain wondered whether the text could not be based on the concept of "earnings" instead of "activity", which would be relevant when contributions are being paid in different Member States, e.g. that of work and that of residence. The Commission ... will consider reintroducing ... the reference to "earnings" in 1[3](5).<sup>118</sup>

Amendments were also made to the Commission's proposal under the Spanish Presidency of the Council:

In accordance with the Council's instructions of 3 December 2001, the Spanish Presidency has drawn up a new text based as closely as possible on the Commission proposal and introducing certain amendments arising from the approved parameters. It has also inserted some of the suggestions and proposals, particularly those with majority or unanimous backing, which were tabled in the course of the many meetings of the Working Party on Social Affairs.<sup>119</sup>

110. A deviation between a tax treaty and the Regulation could exist if the tax treaty allocates the taxation right on a pension lump sum to the source state, whereas Art. 13(2) of the Regulation designates the social security legislation of the residence state to apply.

111. Regulation (EC) No. 883/2004 of the European Parliament and of the Council of 29 April 2004 on the coordination of social security systems (OJ 2004, L 166/1; corrigendum in OJ 2004, L 200/1).

112. ECJ, Advocate General's Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d'allocations familiales de Paris – Région parisienne (Urssaf)*, footnote 4.

113. Proposal for a Regulation of the European Parliament and of the Council laying down the procedure for implementing Regulation (EC) No. 883/2004 on the coordination of social security systems, adopted by the Commission on 31 January 2006 (COM (2006), 16 final) which will replace the current Implementing Regulation No. 574/72; still not adopted by the European Parliament and the Council.

114. Art. 91 Regulation No. 883/2004.

115. COM/1998/779/final.

116. Common position of 19 January 2004 adopted by the Council with a view to the adoption of a Regulation of the European Parliament and of the Council on the coordination of social security systems (15577/03).

117. Art. 10(5) of the Proposal for a Council Regulation (EC) on Coordination of Social Security Systems of the Commission of 21 December 1998, COM (1998) 779 final.

118. Outcome of proceedings on 14-15 September 1999 of the Working Party on Social Questions of the Council of the European Union of 28 September 1999, 98/0360 (COD), 11331/99, SOC 320, CODEC 515.

119. Proposal of an amended text of the Regulation by the Spanish Presidency of the Council of the European Union of 20 December 2001 to the Working Party on Social Questions of the Council of the European Union, 1998/0360 (COD), 15509/01, SOC 549, CODEC 1393.

One of the amendments was the insertion of the phrase “and were receiving all their income” into the original Commission’s proposal. This phrase was also included in the final version of the new regulation.

A self-employed person, such as Mr Derouin, would fall within the scope of Art. 13(2) of Regulation No. 883/2004. Art. 13(5) of Regulation No. 883/2004 provides that these types of persons are treated as if they receive all their income in the Member State concerned for the purposes of the French legislation. The Advocate General’s Opinion in *Derouin* regards this as the codification of *Allard* into the Regulation.<sup>120</sup> Specifically, the Advocate General interprets *Allard* as follows:

The fact remains, as the Commission has stated, that it follows in particular from the interpretation of Article 14d(1) of Regulation No. 1408/71 given in *Allard* that the Member State whose social security legislation is designated in accordance with Article 14a(2) of Regulation No. 1408/71 must levy contributions falling within the scope of that regulation on the total income of a self-employed person derived from self-employment both in the Member State whose legislation is designated and in another Member State.<sup>121</sup>

As indicated in 6.2., the interpretation of *Allard* by the Advocate General’s Opinion differs from the approach that the ECJ adopted in its judgment in *Derouin*. The inclusion in Regulation No. 883/2004 of the rule that self-employed migrant workers must be treated as if they “were receiving all their income in the Member State concerned” appears to differ from the ECJ’s judgment in *Derouin*. In this respect, the following statement made by the ECJ is relevant:

On the facts of *Allard*, the Member State of residence of the person concerned chose to include in the tax base for social contributions all the income earned by him both on its territory and on that of another Member State, as it was authorised to do so by Regulation No. 1408/71. Given the context, the Court held that, in accordance with the national legislation applicable pursuant to the conflict of law rules of that regulation, the social contributions payable by the person concerned should be calculated taking into account his total income.<sup>122</sup>

If, according to the ECJ in *Allard*, the Member State of residence is *allowed* to choose to include all income into the tax base, Art. 13(5) of Regulation No. 883/2004 *requires* the Member State of residence to include all income into the tax base for social security contributions because they are deemed to receive all their income in the Member State of residence. Art. 13(5) of Regulation No. 883/2004, in combination with the direct effect of regulations<sup>123</sup> would, therefore, require the designated Member State to include foreign-source income in the tax base for social security charges.

## 9. Conclusions

The ECJ reached a totally different conclusion than the Advocate General in *Derouin*. In contrast to the ECJ, the Advocate General concluded that France had to levy the social security contributions at issue (the CSG and CRDS) on the basis of Mr Derouin’s worldwide income under the Regulation. The ECJ correctly decided that France was allowed to exclude UK-source income from

the tax base in calculating the contributions by virtue of the Treaty. The relationship between a tax treaty and the Regulation may also arise in other cases, for example regarding employment income, business profits and pension income. In these situations, the tax treaty may allocate the taxation right on the income to the source state, whereas the Regulation designates the residence state’s social security legislation to apply exclusively. Consequently, the ECJ’s judgment has implications for these situations.

The ECJ concluded that Mr Derouin fell within the scope of the Regulation, as the order of reference and all the observations submitted to the ECJ demonstrated that Mr Derouin had the status of a self-employed migrant worker. As a result, Art. 14a(2) of the Regulation applied, thereby determining that the resident state’s social security applied to Mr Derouin, i.e. France. Mr Derouin, however, argued that he did not perform any professional activities in the United Kingdom, but that he only received the UK-source income as partner of a UK partnership. The United Kingdom did not indicate whether or not it regarded Mr Derouin as a self-employed person under its national social security legislation. If this were not the case, the Regulation and especially the conflict rules of Title II do not apply. This is different for Art. 14 of the Treaty (independent professional services), which assigns to the United Kingdom the right to tax the income attributable to a fixed base that a French resident has regularly available to him in the United Kingdom for the purpose of performing work in an independent capacity. It is not necessary that a person actually performs activities in the United Kingdom for purposes of Art. 14 of the Treaty.

The peculiarity of *Derouin* is that the social security contributions concerned fell within the material scope of both the Treaty and the Regulation, as they similarly met the criteria of “tax” under the Treaty and of “social security legislation” under the Regulation. Generally, social security contributions are not covered by the material scope of a tax treaty, as there is no direct connection between the payment and the benefits to which an individual is entitled. The CSG and CRDS, however, lack such a connection with the individual benefits to be received. As a result, they should be regarded as taxes within the meaning of the Treaty. In addition, the 2004 and 2008 France–UK tax treaties explicitly refer to the CSG and CRDS as taxes within the meaning of these tax treaties. The ECJ, however, adopted another approach for the purposes of the Regulation. Specifically, the ECJ concluded that a direct and sufficiently relevant link was present, as the proceeds from the CSG and CRDS were

120. ECJ, Advocate General’s Opinion, 18 October 2007, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d’allocations familiales de Paris – Région parisienne (Urssaf)*, footnote 35.

121. *Id.*, Para. 52.

122. ECJ, 3 April 2008, Case C-103/06, *Philippe Derouin v. Union pour le recouvrement des cotisations de sécurité sociale et d’allocations familiales de Paris – Région parisienne (Urssaf de Paris – Région parisienne)*, Para. 29.

123. Art. 249 EC Treaty.

employed to finance the social security benefits, which are covered by the Regulation. This conclusion was not altered by the fact that the CSG and CRDS did not give entitlement to any direct and identifiable benefit in return. According to the authors, the rationale behind the approach adopted by the ECJ is the definition of social security legislation in Art. 1(j) of the Regulation, which requires a relationship between “regulations and other provisions and all other implementing measures” (including charges) and “branches and schemes of social security”. Even though the ECJ’s approach is supported by the wording of Art. 1(j) of the Regulation, the authors are of the opinion that it is not an appropriate criterion to determine the connections in *all cases*. Taking the view that the connection with the individual benefiting from the social security is unimportant may result in situations in which indirect taxes could also be characterized as social security levies when the revenues were hypothecated to social security benefits. Accordingly, the authors are of the opinion that the ECJ’s approach is *only* effective in the case of direct taxes levied from individuals ultimately benefiting from the social security system.

In *Derouin*, the question arises as to whether the Treaty should be classified under the Regulation as (1) national social security legislation or (2) a social security convention. According to the authors, the Treaty cannot be characterized as a social security convention because it (1) only concerns the levy of taxes, (2) does not directly provide benefits to individuals stemming from funds to which that tax treaty may apply and (3) lacks other elements of social security conventions. The ECJ in *Derouin* did not devote explicit attention to the various features of classifying or not classifying the Treaty under the Regulation. Nevertheless, the ECJ simply characterized the Treaty as national legislation, thereby allowing its application.

On several occasions, the Advocate General’s Opinion in *Derouin* referred to new Social Security Regulation No. 883/2004. This will replace the Regulation. Art. 13(5) of Regulation No. 883/2004 in combination with the general principle of direct effect of regulations on the basis

of Art. 249 of the EC Treaty appears to require the Member State of residence to include all income into the tax base for social security contributions.

One of the major principles underlying the Regulation is the single state principle, i.e. the authority to levy social security contributions is assigned to only one Member State to the exclusion of the other. In addition to the single state principle, some scholars also recognize the principle of overriding effect underlying the Regulation. To the authors’ knowledge, the ECJ’s decisions did not explicitly recognize the principle of overriding effect.

Another question is whether Member States could totally forgo the levy of social security contributions under their national legislation or a tax treaty. In *Derouin*, the ECJ emphasized the principles underlying the Regulation. The ECJ did not refer to the principle of overriding effect. The Court only explicitly referred to the single state principle. The ECJ also referred to the provisions on non-discrimination and free movement. This may imply that the principle of overriding effect does not underlie the Regulation. The ECJ clearly distinguishes between social security *benefits* and social security *contributions* with regard to the competent Member State’s obligations under the Regulation. These Member States cannot deprive the individual of his right to receive social security benefits. A Member State is, however, free to decide whether or not to levy social security contributions and to calculate these contributions. Consequently, assuming that the Regulation is, indeed, based on the principle of overriding effect, in the authors’ view, this principle does not require the Member States to levy social security contributions and they can even forgo, unilaterally or via a tax treaty, the levying of these contributions.

Finally, the ECJ in *Derouin* demonstrates that a tax treaty and the Regulation may be applied simultaneously. This simultaneous application has the following advantages for the individual concerned: (1) the Regulation guarantees social security benefits and (2) a tax treaty may result in a reduction in the social security contributions due.