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Double Taxation Conventions and Social Security Conventions

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I. General Part

1. Comparison of the National Social Security Systems and Tax Systems

1.1. Characteristics of the German Social Security System

As the Bismarck model of social security was developed in Germany, the German social security system is based upon Bismarckian principles even today. This means that social security is concentrated on wage-earners. In contrast, some groups of the self-employed and public employees are protected by special systems which are organised separately from the general social security system as independent institutions.

The general social security system is based on the concept of social insurance. The persons covered are treated as insured persons, are obliged to pay income-related contributions and – as cash benefits are concerned – are entitled to income-related benefits. The social security systems are predominantly financed out of contributions. However, there are "non-insurance based" expenditures of the social security schemes, e.g. maternity benefits, benefits for childbearing or benefits to German nationals who came to Germany from a country in Central or Eastern Europe with which Germany did not have a SSC in the past, that are paid out of transfers stemming from the general budget.

In essence, the German social security system represents the archetype of the Bismarck model until today.

1.2. International Dimensions of German Social Security Law

As to the international scope of application, the German social security system is based on a combination of principles. For social benefits in general, German law applies to all persons who are domiciled in Germany (§ 30 SGB I). For social insurance benefits, however, German law applies to all persons who regularly execute their work as an employee or as a self-employed person in Germany (§§ 3 et seq. SGB IV). Since the place of residence or the workplace is determined as the key connecting factor, "territorial" links prevail in German international social security law. Nationality is a connecting factor of shrinking importance. Today it has only a residual function – above all in relation to those persons who, as members of the German ethnicity, were resident in former communist

states and were allowed to immigrate to Germany ("*Spätaussiedler*"). On this legal basis, hundreds of thousands of migrants have moved to Germany every year since the mid 1970s. As regards their pension rights acquired under the legislation of their previous state of residence and/or employment, these persons are compensated by Germany due to the lack of SSCs and the inadequacy of their benefit rights acquired in their previous state of employment and/or residence.

1.3. General Characteristics of the German Taxation System

The German system of taxation is built upon two pillars – direct and indirect taxation. The income of both individuals and corporations is subject to direct taxation. It is subdivided into income ("*Einkommen-*") and corporation ("*Körperschaft-*") tax ("*Steuer*"). Income tax is levied on a progressive basis, which means that the tax rate is rising the higher the income is.

The transfer of goods and services in exchange for money and the use of energy form the basis of indirect taxation. The first type is the sales tax ("*Umsatzsteuer*"); the latter is the energy tax ("*Ökosteuer*").

As a rule, tax liability is connected to permanent residence in Germany. However, persons residing outside Germany may be subject to taxation if they acquire certain types of income within the German territory, e.g. from business, capital or rent and lease.

There are various points of contact between the German tax and social security system. There are tax benefits that are awarded for social contingencies such as having a family. The most prominent, though heavily criticised example is the tax-splitting among spouses, which means that taxation is based on the household income rather than on individual earnings. Secondly, there is a tax deduction for the costs of child-raising, covering alimony, the costs of institutional child care and education. Thirdly, a child allowance is either granted in cash or – for parents with a permanent residence in Germany and unrestricted tax liability – in form of a tax allowance. The latter has been introduced to keep the subsistence minimum for families untaxed.

2. Personal and Material Scope of SSCs and DTCs

2.1. SSCs

The SSCs concluded by Germany in the past dealt with different problems emerging from the very fact of cross-border contacts of substantial relevance. The first conventions can be traced back until the beginning of the 20th century when – due to a lack of qualified workers – migrant workers from countries such as Italy, France, Serbia and Croatia had been recruited to work in Germany. Further cross-border contacts emerged during the Nazi era when Germans immigrated to other countries due to the Nazi persecution. After World War II, SSCs were concluded to provide for an adequate protection of frontier and migrant workers moving to Germany since the mid 1950s on the basis of bilateral treaties. The SSCs are based upon model treaties which were in the last consequence embedded in ILO-Conventions on the formation of SSCs, which date back to the 1920s and 1930s. In that period, the ILO enacted a series of recommendations and conventions on the characteristic principles of SSCs, the most crucial ones being convention No. 19 and 48 as well as recommendation No. 2; and convention No. 118 and 157 after World War II. In the history of after war (West) German SSCs, the contracts with the ("western") neighbour states set the starting point. They were concluded to solve the problems emerging from frontier work, which was common after World War II.

These SSCs were also made to cope with the consequences of labour carried out by nationals of the contracting states during and immediately after World War II. A further series of SSCs were concluded during the 1960s to accompany the international agreements on the recruitment of so-called guest-workers ("*Gastarbeiter*") who mainly came from Turkey, Yugoslavia, Spain, Italy and Greece. In the 1970s, SSCs were concluded with those states which gave permanent residence to the victims of racial persecution during the Nazi period (USA, Canada and Israel). The main intention of these SSCs was the restructuring of pension rights which could not be earned under German law since Jews were excluded from social security during the Nazi era (from 1935 to 1945).

The academic literature is not deeply committed to the subject matter of SSCs.[1] Importance of SSCs is shrinking due to the formation of the EEC, EC and EU. Since E(E)C and EU law is paramount to the national laws of the Member States, EC co-ordination law on social security replaces the SSCs concluded between Member States. According to this phenomenon, the relevance of the SSCs among EU Member States is restricted to social security rights acquired at a time before the relevant state became member of the E(E)C or EU. The case law of the ECJ on the relationship between E(E)C- and SSC-co-ordination rules[2] is not only respected by the German social security administration, moreover many of the relevant cases[3] referred directly to the German system of social security. As to the case law of the ECJ, dozens, presumably nearly a hundred of judgements referred to the German social security legislation.

2.2. The Current Status of SSCs

In 2005 Germany has SSCs with all EU and EFTA countries as well as Switzerland, additionally with Bosnia-Herzegovina, Bulgaria, Chile, China, Israel, Japan, Canada, Korea, Croatia, Morocco, Macedonia, Poland, Quebec, Serbia and Montenegro, Romania, Slovenia, Turkey, Tunisia and the USA.

There is also a substantial amount of case law referring to the main provisions. For each of the various SSCs, the highest (Federal) Social Security Court ("*Bundessozialgericht*" = BSG) issued a series of judgements. The most controversial issue during the last decades originated from the question whether the provisions of two or more SSCs have a multilateral effect.[4] The same problem can be identified in EU case

1 Rolf Schuler, *Das internationale Sozialrecht der Bundesrepublik Deutschland*, 1988; Eberhard Eichenhofer, *Internationales Sozialrecht*, 1994; Plöger/Wortmann, *Deutsche Sozialversicherungsabkommen mit ausländischen Staaten*; Ulrich Petersen, Sozialversicherungsabkommen, in von Maydell/Ruland, *Sozialrechtshandbuch*, 2003, MN 34; The interaction of international tax law and international social security law has been dealt with by Klaus Vogel, Internationales Sozialrecht und Internationales Steuerrecht im Vergleich, in *Festschrift für Zacher*, 1998, p. 1173.

2 ECR 1973 – 599 (*Walder*), 1975 – 1149 (*Petroni*), 1991, I-323 (Rönfeldt), 1993, I-4505) (*Grana-Novoa*), 1995, I-3813 (*Thévenon*), 1998, I-2461 (*Rodriguez*), 2000, I-9399 (*Thelen*), 2002, I-1261 (*Kashe*).

3 ECR 1991, I-323 (*Rönfeldt*), 1993, I-4505) (*Grana-Novoa*), 1995, I-3813 (*Thévenon*), 1998, I-2461 (*Rodriguez*), 2000, I-9399 (*Thelen*).

4 For more detailed information cf. the section on anti-discrimination clauses (II.1.3, p. 333 et sequ.).

law. Whereas the ECJ held in the case "Grana-Novoa"[5] that the provisions of EU co-ordination law and SSCs cannot be applied cumulatively, it overruled this principle in the "Gottardo" judgment.[6]

As to the relevance of the SSCs in relation to EC law, we can observe a shrinking importance of the first compared to the latter. Due to Art. 6 of Reg. (EEC) 1408/71, the EC co-ordination law is paramount to national legislation and the SSCs concluded by the EU Member States. At the same time, the territorial scope of application of EC law is expanding due to the enlargement of the EU and the EU/EEA Member States.

The structure of Reg. (EEC) 1408/71 will be maintained under the new Reg. 883/2004. Therefore, in the transition from the current to the future legal framework, the personal scope of both regulations will be determined in the same manner. In general, the same holds true for the material scope of the co-ordination rules. There is only a tiny revision, in so far as interim payments of the state to advance lacking payments of alimony to children have no longer to be conceived as social security benefits.[7]

There is no general rule which allows determining the material scope of SSCs. The answer to this question depends on the political purpose a SSC has to fulfil. For example, the SSCs between Germany and the USA and Canada were concluded to preserve pension rights. Consequently, the material scope of these SSCs is limited to pensions. The German-Turkish SSC, in contrast, was concluded to integrate the migrant workers coming from Turkey to Germany adequately into the German social security system. Thus, the central matters of "social security" (within the meaning of the EC legislation) are covered: invalidity, old age and survivor pensions, work accident and professional disease benefits, health insurance and family benefits. Only the unemployment insurance benefits are lacking.

The German SSCs are relevant for both benefits and contributions. Given that all SSCs determine the international scope of application of the contracting states' social security legislations in relation to each other, there is only one state competent. This technique embraces the authority of the other contracting state to levy contributions. The main emphasis in

5 ECR 1993 I-4505 (*Grana Novoa*).

6 ECR 2002 I-413 (*Gottardo*).

7 Statutorial revision of ECR 2001, I-2261 (*Offermanns*), ECR 2002, I-1205 (*Humer*).

SSCs, however, is given to the co-ordination of benefits. Their main target is to overcome the restrictions embedded in national social security legislation and to strengthen the international effectiveness of social security rights established under the legislation of one Member State. These restrictions refer to residence clauses as to payments of benefits in cash, the disregarding of credits acquired under the legislation of another Member State and, finally, the restriction that benefits in kind are accessible only to those covered by the legislation of the competent state.

2.3. International Scope of German Taxation Law and DTCs

As far as the taxation of income is concerned, the taxation under German law is directed to the acquisition of income of persons who work as employees or are self-employed in Germany. The corporation tax is payable by all corporations that have their legal seat in Germany. Sales tax is levied under German law if a transaction takes place in Germany. A fundamental distinction is made for income taxation as to the residence of the taxpayer. If income is earned for an economic activity carried out in Germany, we must distinguish between "unlimited" and "limited" taxation ("*unbeschränkte / beschränkte Steuerpflicht*"). This distinction refers to the extension of taxable income. In a system of "unlimited taxation", the fiscal authority levies taxes on each income the taxpayer has earned world-wide. However, under a regime of "limited taxation", the levying of taxes is restricted to income earned in Germany. Persons who work and live in Germany are exposed to unlimited taxation. Persons who work in Germany but live abroad are, however, subject to limited taxation. Thus, the German taxation law bears both a territorial and a personal reference.

If these rules are internationally common – which, in fact, they are – these two principles give rise to the danger of double taxation. Under these rules, an income can be taxed by more than one state. Such cumulative taxation would be detrimental to taxpayers who have links to various states, for example because they reside in one state but earn their income in another. Thus, their income would be submitted to the taxation of both the state of residence and the state of work. In order to avoid double taxation in this case, DTCs are concluded.

Based on an OECD[8] as well as a UN[9] Model Convention, Germany has implemented DTCs with more than 80 states at this moment. The UN Model Convention formed the basis for conventions concluded between Germany and developing countries. Although the various DTCs are not identical – due to some peculiarities contained in each of them – their structure is alike. DTC protection is provided for residents in at least one of the contracting states. The ECJ has held that the scope needs to be extended to cover not only persons but also permanent establishments of enterprises.[10]

DTCs are based on the principle that different types of income (e.g. income from land, entrepreneurial activity, work, shares, pensions, public employers) are taxable by one of the contracting states to a certain percentage. The tax paid for income in the tax-levying state can be deducted from the tax to be paid in the other contracting state. The right to subtract foreign taxes from home taxes avoids that the same income is taxed twice.

Normally, the DTCs are relevant for the direct taxation of income only. Other taxes are covered only if they are explicitly listed in the treaty. DTCs do not cover indirect taxation.

Social security contributions are not levied by tax authorities but by the social insurance bodies. In Germany these are the health insurance bodies that collect the contributions paid to other social insurance branches as well. Since the payments to social insurance institutions are earmarked – solely meant for the financing of social security benefits – social security contributions are not considered as taxes within the meaning of Art. 2 of the OECD Model Tax Convention on Income and Capital (OECD MC). It is one of the main characteristics of a "tax" that its revenues become part of the general budget of a state, which can be used to finance any task of public interest.

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8 *OECD Model Tax Convention on Income and Capital*, referred to by Klaus Vogel, *Doppelbesteuerungsabkommen der Bundesrepublik Deutschland auf dem Gebiet der Steuern vom Einkommen und Vermögen*, 2003.

9 *United Nations Model Double Taxation Convention between Developed and Developing Countries*, referred to by Harald Schaumburg, *Internationales Steuerrecht. Außensteuerrecht. Doppelbesteuerungsrecht*, 1998; Klaus Vogel, *Doppelbesteuerungsabkommen der Bundesrepublik Deutschland auf dem Gebiet der Steuern vom Einkommen und Vermögen*, 2003.

10 ECR 1999, I- 6161 (*Saint-Gobain*).

As regards the question whether the financing of social benefits out of taxes or contributions would make any difference in subsuming social security contributions under the notion of "tax" as used in the OECD MC, the answer is definitely positive. The main differences can be seen in the basis, the rate and the international scope of taxation. As to the basis, contributions are levied on income from work. Taxes, however, can be levied on income deriving from all sources. As to the rate, financing on the basis of contributions implies a constant rate (which might be lowered for earners of low income). In contrast to the foregoing, financing on the basis of taxes is usually based on a flexible rate, which varies depending on the amount of income. Finally, as to the international scope of application, the difference stems from the fact that the levying of contributions is addressed to persons working in the imposing state whereas taxation is based on the permanent residence of the taxpayer.

As to the ECJ judgement on the French *contribution généralisée de sécurité sociale (CSG)*,[11] the ECJ has stated that this means of financing social security cannot be qualified as a tax but rather as a social security contribution. Of course, one has to affirm that it is in the sole responsibility of the Member States to define the notions of "tax" or "contribution". However, it has to be ensured that national legal rules are applied uniformly in cases with international reference. The mere fact that national law defines a fiscal source as "tax" or "contribution" can thus not be the only criterion for its qualification in a cross-border context. Keeping this in mind, the ECJ decision cannot be questioned: the levying of the CSG is based upon the French rules on social security contributions. Moreover, the revenue is absolutely restricted to the purposes of the social security system in so far as the CSG is intended to "subsidise" the regular social security contributions levied on income from work. As an earmarked tax it is thus not a tax in the strict legal sense but a contribution to finance social security. In our view, it is therefore clear that one cannot speak of a tax in this case.

[11] ECR 2000, I-995 (*Commission vs. France*); ECR 2000, I-1049 (*Commission vs. France*).

3. Distributive Rules and Co-ordination of Benefits

Whereas DTCs subdivide the taxation power between two contracting states, SSCs do not distribute responsibilities themselves. Their main emphasis is put on the waiving of barriers for the maturation and verification of the beneficiary's rights. Thus, the characteristic coordinative provisions of each SSC are: the equal treatment clause, the provision on the exportation of benefits in cash, the aggregation of credits-clause, the granting of access to benefits in kind and, finally, administrative provisions on the implementation of these coordinative rules.

The DTCs' distinction between distributive and method articles cannot be found in SSCs because SSCs do not share taxing powers but order social security administrations to broaden the effectiveness of social protection embedded in the legislation of one contracting state. A certain similarity of distributive rules in DTCs and SSCs can be found in those types of SSCs which have been enacted to take over credits under the legislation of one contracting state by the other. Those SSCs were quite common in the past. The origin and purpose of such arrangements lie in the changes of territories and the compensation of losses in connection with social protection caused by forced labour. This feature prevailed as a means of burden-sharing for migrant workers in the communist era. Workers covered by the social security legislation of the sending state kept their protection while working in another state. This solution is based upon a generous interpretation of the rules on posting that are inherent in the common SSCs.

In the context of SSCs residence is not relevant. However, it has importance for the administration of tax financed social benefits. As to § 30 SGB I, the entitlement to social benefits – which do not qualify as social security or social insurance benefits – is restricted to persons who have their permanent residence in Germany. The notion of "permanent residence" refers to a location around which the individual's life centres. This concept concurs with the concept of residence to be found in DTCs.

The SSCs are based upon principles which are internationally widely accepted. These principles also form the basis of the EU co-ordination legislation as laid down in Reg. (EEC) 1408/71 or Reg. 883/2004. Both systems of co-ordination are subject to different principles for benefits in cash and in kind. These differences can be explained by the different

nature of the type of benefits concerned: Benefits in cash focus on the waiving of restrictions on exportability and on the determination of rules to ensure that the transfer of cash becomes effective. For benefits in kind, however, coordination has to ensure that a person covered by the legislation of another state has access to the services offered in the state if the need arises.

As to the overall aim of avoiding a double levying of social security contributions, it has to be noted that this aim is difficult to achieve even within the EU. The judgements in the ECJ-cases of "Fitzwilliam"[12] and "Banks"[13] indicate this phenomenon quite clearly. The same is the case in the context of SSCs. There, similar problems have to be solved if no international instrument is in place – leading to the consequence that a double levying of contributions cannot be prevented – just like double taxation takes place in the absence of a DTC.

4. Interpretation and Qualification Conflicts Concerning SSCs and DTCs

In order to avoid or to solve conflicts of qualification related to SSCs, a board of representatives of the relevant states is established to solve such disputes – comparable to the Advisory Committee on Social Security for Migrant Workers under EC law (Art. 80 Reg. (EEC) 1408/71). Additionally, due to an elaborated system of legal control, conflicts on the interpretation of the key terms of SSCs are submitted to the judicial supervision of independent courts.

As to DTCs, Art. 25 OECD MC holds that tax payers may present their case to the competent national authorities of either their state of residence or the state of their nationality in case they feel not treated in accordance with the DTC. In case of any dispute over the interpretation or application of the DTC, the contracting states, however, shall endeavour to resolve a conflict by mutual agreement. In general, the Vienna Convention on the Law of Treaties is recognised as an international custom for the interpretation of unclear terms. Additional reference can be drawn from the list of definitions contained in Art. 3 OECD MC – even though this article contains the problematic clause that the definitions in the legislation of the applying state are relevant "unless the context otherwise

[12] ECR 2000, I-883 (*Fitzwilliam*).
[13] ECR 2000, I-2005 (*Banks et al.*).

requires". This rule provides for flexibility of interpretation, but it is not clear which starting point needs to be chosen regarding the term "context". Similar clauses are contained in the DTCs Germany has concluded with the United Kingdom and Australia. In German academic literature this question has not been dealt with in detail. It is not considered to be a significant problem of interpretation but a mere tool to enlarge the scope of discretion for courts dealing with DTC provisions. In practice, no disputes have arisen from these clauses.

Qualification conflicts under SSCs arise from time to time. Despite the existence of those conflicts, the main origins of conflicts are not different views on the interpretation of the SSCs between different national administrations but between administration and the beneficiary. These disputes are regularly solved by a court ruling. Its task is to provide a binding interpretation of the SSCs. Given that different courts of the same state and level may assess SSCs differently, a full and binding interpretation is to be provided by the ultimate instance, which is the Federal Social Security Court ("*Bundessozialgericht*") in Germany. Such legal actions can be avoided by a preliminary administrative procedure which has to take place before court proceedings. If a beneficiary is not convinced of an administrative ruling, she/he can ask for a reconsideration of the decision by the administrative body that has made the decision. In this procedure the conflict can be solved – but only if the administration accepts the SSCs' interpretation given by the beneficiary.

As Germany is a member of the EU, the interpretation of Reg. (EEC) 1408/71 by the Advisory Committee on Social Security for Migrant Workers is carefully studied and respected by the representatives of the administration. Besides, interpretation conflicts may be solved by referring to the list of definitions contained in Art. 1 of the Regulation. This list, however, may lead to problems: some of the definitions contained, e.g. on the notion "worker", may vary throughout the different Member States since it refers to the national legislation on social insurance.

As a general rule, one focuses on a teleological approach when interpreting provisions. The main aim in applying SSCs is to achieve their purpose, i.e. to give priority to free movement of workers and to justify any restrictions of the rights granted in the EC Treaty. Of course, the EC Treaty's principles need to be observed when interpreting DTCs, too.

II. Special Issues

1. Specific Provisions

1.1. Cross-border and Posted Workers

Both SSCs and DTCs are concluded to address and solve the problems of cross-border work and the posting of workers. Getting along with cross-border work originally gave reason to enact SSCs. In Germany with its historically explainable and justified preference to a work-oriented system of social security, SSCs lay down the principle that cross-border workers are covered by the social security system of their regular state of work. For such a provision to become an adequate instrument of protection for the cross-border worker, SSCs contain rules to safeguard security in their states of residence. The most important instrument for benefits in cash is exportability. It waives all restrictions enacted in national legislation as to the payment of social benefits to a beneficiary residing outside the competent state. For benefits in kind an adequate provision is implemented by giving access to all service providers based in the state of residence. Finally, for benefits based on credits acquired in the sequence of time due to coverage as an insured – worker or resident – SSCs allow for an aggregation or totalisation of credits acquired under different national legislations which finally leads to the determination of entitlement to benefits.

For posted workers, the German legislation provides in §§ 4 – 5 SGB IV that a worker who is regularly active in Germany preserves her/his social security status even if she/he works temporarily abroad. Vice versa, a worker who is temporarily active in Germany and, at the same time, is regularly active in another state, is covered by the social security legislation of the state of her/his regular employment. For DTCs, taxation is based upon the permanent residence in Germany. If there is a residence in Germany, the income earned is taxable irrespective in which state an acquisition takes place. Taxation does therefore not depend on a work contract in Germany. Workers with a permanent residence in a foreign state are taxable with their income earned in Germany. Even income earned in a third state is taxable if its economic effect takes place in Germany (§ 49 para. I No. 4 EStG).

Therefore, SSCs and DTCs are based upon a fundamental difference in their key connecting factor: Whereas SSCs are built upon the *lex loci*

laboris-principle, DTCs are based on the *lex domicilii*-rule. According to Art. 15 OECD MC, there is room for taxing income earned from employment by the authorities of the source state if a worker is residing in that country not longer than 183 days within a 12-months period.[14] Otherwise, the state of residence taxes the income earned abroad.[15] Social security protection and taxation, hence, differ for both cross-border and posted workers. Generally speaking, there is a split of competences for cross-border workers, which is not the case for posted workers. This split occurs if the period of temporary work outside the states of the regular employment has expired and the worker keeps her/his permanent residence in the state of his/her previous employment. Accordingly, cross-border workers are subject to taxation in the state of their permanent residence. At the same time they are committed to pay contributions in the state of their regular employment.

Predominantly in the border regions between Denmark and Germany, a cumulation of financial burdens due to profound differences in the financing of social protection in these two countries brings about that residents of Denmark and workers in Germany bear a double burden. This is due to the difference between Germany with a strong commitment to contribution financing and Denmark with a strong orientation towards tax financing. However, only a small percentage of cross-border workers are subject to such a de facto cumulation of financial burdens. There is no evidence to confirm the hypothesis that there is a financially driven movement from a contribution to a tax based system of social security.

As Germany has been member of the EU since nearly half a century, the case-law of the ECJ[16] is respected. In public opinion, however, this principle is not widely acknowledged yet. Above all, in those regions where Germany has a joint border with Poland or the Czech Republic, the economic activities of service providers domiciled in these countries and active in Germany cause a deep political concern in the German public opinion, mainly due to huge differences in wages and social security levels.[17]

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14 Klaus Vogel, *Doppelbesteuerungsabkommen*, 1990, Art. 15 OECD MC, Rn. 4.

15 Ibid., Rn. 17 and 88 et seq.

16 ECR 2000, I-883 (*Fitzwilliam*); ECR 2000, I-2005 (*Banks et al.*).

17 Cf. the jurisdiction on letterbox companies: ECR 1999 I-1459 (*Centros*); ECR 2000 I-9379 (*Plum*).

1.2. Pensions

If a pensioner entitled to benefit under German law does not reside in Germany but abroad, the pension will be paid without restriction if the beneficiary is a German citizen. Pensioners with a foreign citizenship have to accept a cut of their pension: the non-contributory elements of the pension are not to be exported at all and the contributory element of the pension is only payable to 70 per cent of the amount due if the beneficiary stayed in Germany.

SSCs and EU coordination rules set this cut-back of pensions for non-Germans aside. They safeguard the unrestricted export of pensions irrespective of the pensioner's residence and citizenship and irrespective of the nature (contributory or non-contributory) of the pension right. Again, SSCs and DTCs are based upon different rules and principles. Whereas SSCs are based on the *lex loci laboris*-rule, the DTCs follow the *lex domicilii*-rule. Hence, DTCs are based on the residence principle, which means that pensioners are subject to taxation in the state where they have their permanent residence.

The SSCs provide for a calculation of pensions based on credits acquired under different pension laws according to the proportional share of the right earned under the legislation of one state in relation to the period of coverage during his/her whole insured life. This requires an aggregation of insurance periods acquired in both contracting states. For the determination of waiting periods, the sum of all acquired periods in all states where the pensioner has worked is taken into account. The payable amount is calculated according to the legal provisions of the respective state and the proportions of pensions acquired under the legislation of each state are added *pro rata temporis*. European law, on the contrary, requires two steps for the calculation of pensions: first, the theoretical amount of a pension has to be determined in compliance with the procedure described above. Additionally, a second calculation method has to be carried out: the calculating state has to figure out the amount of pension acquired solely under its own legislation. EU law requires that the results are compared on the basis of both methods and the higher amount is paid.

Due to the different connecting factors of SSCs and DTCs, the statutes of social security protection and taxation differ if persons moved during their work-life or after the termination of their work and took residence in

another country. This may give rise to the risk of a double tax burden if the worker is covered by the social security scheme in a state where contributions are taxed, i.e. levied on gross income, and moves to a country where pensions are taxed after reaching pensionable age. On the other hand, loopholes in taxation may occur if a worker pays untaxed contributions in the country where she/he is covered by a social security scheme and moves to a country where pensions are not taxed either. Solving this problem is a task of DTCs. The conventions that Germany has concluded, however, do not tackle this problem.

The administration of pension payments based upon an international work history does not give rise to substantial problems, because the competence to administer the pension rights is concentrated in highly specialised agencies within the pension administration in all the relevant cases. Smaller problems deal with the calculation of pensions if the amount is payable in another county. This is the case if the beneficiary is residing outside the EURO zone. In this case the exchange rate of the EURO to the currency of the state of residence can vary. That is why the exchange rate is to be fixed periodically.

The DTCs' administration is confronted with the problem of changes in exchange rates either. Here the administration can refer to the regularly fixed exchange rates, too.

1.3. Anti-Discrimination Clauses

Both DTCs and SSCs prohibit any discrimination based on an individual's nationality. This clause makes any distinction in taxation or social security based on the nationality of the taxpayer or the socially insured person unlawful. The substantial scope of these clauses is restricted to the subject matters of taxation and social security – understood in the ambit defined by the provisions on the substantial scope of SSCs and DTCs.

The principle of non-discrimination among the persons covered because of their nationality is a corner stone of EU social security coordination law.[18] In both the SSCs' and DTCs' understanding not only direct, but also indirect discrimination is forbidden. Indirect discrimination is initiated by a provision which does not formally discriminate against citizens of other Member States, but has this effect in reality, without giving sufficient

[18] Cf Art. 12 EC, Art. 3 Reg. (EEC) 1408/71, 4 Reg. 883/2004.

justification to the difference, which has nothing to do with the differences in nationalities.[19]

One important issue is the question whether the provisions of two or more SSCs may have a multilateral effect. It has been severely controversial whether the principle of non-discrimination demands that bilateral SSCs have to be extended to residents or nationals of other EU Member States. In Germany the discussion took place at the beginning of the 1980s. The German social security administration constantly neglected the multilateral effect by referring to the bilateral character of the SSCs. The BSG, however, held that the bilateral character was relevant only in relation to the contracting states since they were not allowed to oblige other countries that were not parties to the convention.[20] It affirmed the multilateral effect of SSC provisions on nationals of other Member States, since the aim of SSCs – the strengthening of pension rights of claimants migrating within the EU – would be set aside if no multilateral aggregation of pension periods took place. As a consequence of this jurisdiction, special clauses were included in German SSCs which explicitly exclude the extension of their personal scope of application to nationals of other countries (so-called "Abwehrklausel"). These clauses were affirmed by the BSG. The court respected the will of the contracting parties and their unique right to determine in how far contributory periods completed in foreign countries shall be relevant under their national law.

In 1993 the BSG referred a case to the ECJ ("Grana-Novoa")[21]. In this case, a Spanish citizen who had been working in Switzerland and Germany claimed a disability pension in Germany. The social security administration denied her claim because she had not fulfilled the necessary waiting period according to German law, which would have been the case if her contributory periods in Switzerland had been taken into account. This had been rejected because the scope of application of the German-Swiss SSC was limited to German and Swiss citizens. Mrs. Grana Novoa claimed a violation of the non-discrimination principle in Art. 3 of Reg. (EEC) 1408/71, which demanded that she should be treated as if she was a German citizen. In its judgement, the ECJ denied

[19] Cf. only ECR 2001, I-5363 (*Vanbraekel*), ECR 2001, I-5473 (*Geraets-Smits/Peerbooms*).

[20] BSGE 34, 90; 51, 5; 51, 186; 57, 23; BSG SozR 6555 Art. 34 Nr. 1, 2200 § 1250 Nr. 11.

[21] ECR 1993 I-4505.

discrimination on grounds of citizenship. It held that Art. 3 of Reg. (EEC) 1408/71 covered transnational careers completed in EU Member States only, since the Regulation provides for a closed framework of co-ordination rules that is not enlargeable by combining its rules with co-ordination rules of other international instruments. Therefore SSCs concluded with other countries would not fall within its scope.

In 2002, the ECJ overruled this position in the "Gottardo" judgement[22]. In that case, a French woman who had been working in Italy, Switzerland and France claimed an old age pension in Italy. The pension was not awarded since the waiting period required by Italian national law had not been completed. Mrs. Gottardo demanded the aggregation of pension periods that she had fulfilled in Switzerland according to the provisions of the Swiss-Italian SSC. This had been rejected with reference to the claimant's French citizenship. This time, the ECJ clearly affirmed a violation of the antidiscrimination rules. The principle of equal treatment requires that not only citizens of the contracting states may benefit from a multilateral aggregation of periods. Also the safeguarding of the right to free movement as established in Art. 39 EC demands that Member States ensure equal treatment of all EU citizens. Thus, the ECJ disapproved its purely technical argumentation of the "Grana Novoa" case.

Even though the multilateral aggregation is cumbersome from a technical perspective, from a political point of view it is desirable to establish a network of co-ordination rules as global as possible. Administrative bodies are thus not allowed to abstain from an equal treatment clause in one instrument and to impose a different treatment under a second international instrument. Hence, also a cross-over of provisions embedded in different international instruments has to be respected.

Only recently, the ECJ has decided a case concerning the most-favourable-nation principle in tax law.[23] In that case, Mr. D – who is residing in Germany but holds 10 % of his fortune in the Netherlands – has claimed a tax rebate on the Dutch wealth tax. According to Dutch national law, this allowance is granted to Dutch residents only. The Belgian-Dutch DTC however, extended the scope of application of this allowance to Belgian residents. Mr. D claimed a violation of the non-

[22] ECR 2002 I-413.

[23] ECJ, C-376/03, 5. 7. 2005; cf. the annotation of Otmar Thömmes, *IWB* 2005/14, Fach 11a, 887.

discrimination principle as regards the right to free movement of capital in Art. 56 and 58 EC. The ECJ rejected Mr. D's claim and held that the Netherlands were not obliged to grant the tax rebate to citizens of other Member States who held the majority of their fortune in their country of residence. The scope of the Dutch-Belgian DTC does not have to be extended to German citizens. At first glance, the approach of the ECJ in the D case seems to differ fundamentally from the "Gottardo" judgement. However, the two cases are not comparable. The main argument of the court in the D case was that residents and non-residents are in a completely different situation as regards direct taxation: if the major part of income is held in the state of residence, this state has the closer link to award tax allowances. Moreover, this country usually has the necessary information on the taxpayers' situation to verify their entitlement to tax rebates etc. Due to these differences, one cannot speak of discrimination. The most-favourable-nation principle does not demand the application of DTCs to persons who are not citizens of the contracting parties. This is a consequence of their bilateral character. Mr. D did not have a sufficient link to the scope of the Dutch-Belgian DTC because he held only 10 % of his fortune in the Netherlands. The court's arguments in the "Gottardo" case are not transferable to the situation of Mr. D. The latter case dealt with a trilateral constellation while only two EU Member States were involved in the "Gottardo" case. Moreover, both cases are dealing with different areas of law which pursue different aims: international social security law – including SSCs and the EU coordination rules – aim at hindering the loss of social security entitlements due to migration within the European Union. International tax law, on the other hands, seeks to avoid double burdens or loopholes in taxation that might be caused by the free movement of capital. Mr. D did not claim any discrimination in that regard but he claimed a privilege. The right to award such privileges in taxation, however, lies exclusively with the state that has the closer link to the fortune, i.e. the state of residence.

1.4. Dispute settlement

As to the dispute settlement, similar structures are to be observed in both SSCs and DTCs. Whereas DTCs give room for the juridical settlement of conflicts between the individual and the tax administration of one state, SSCs contain dispute settlement clauses to submit different views on the interpretation of SSCs to an arbitrary body. This body provides binding

interpretation in the absence of an international adjudication procedure. The dispute settlement in SSCs does not prevent courts of the competent state's administration from finding a proper interpretation of the law of one state, the incorporated SSCs therein included.

The dispute settlement goes smoothly ahead, because each contracting state can initiate a procedure. Yet, as far as DTCs are concerned, the risk of diverging decisions on the same issues may raise due to the fact that the national courts and authorities decide about their application in this respect. The reason for this can be found in Art. 3 OECD MC, which refers to the domestic law of the applying state when interpreting treaty issues. On the other hand, Art. 23 OECD MC safeguards a uniform handling of questions that have been decided by a national court since it states that such decisions are binding upon the other contracting party.

As regards the information exchanges rules, huge similarities can be noticed between SSCs and DTCs as well. The SSC provisions substantially concur with those of the EU co-ordination law, because both types of provisions establish principles of international administrative law. In any case, it is not possible to transfer information from social security boards to taxation authorities for reasons of data protection and secrecy since the data have been collected exclusively for social insurance purposes.

Generally, efficient dispute settlement requires administrative cooperation, though based on international instruments. As regards matters of social security coordination, Regulation (EEC) 1408/71 has established an Advisory Committee as an international institution for dispute settlement. This board, which consists of representatives of the social partners, examines general questions arising from the implementation of the Regulation and makes proposals for its amendment. The Administrative Commission, on the other hand, consists of representatives of the Member States' governments. It has the power to issue recommendations and solve interpretation conflicts, though it cannot adopt binding decisions. This competence is left to the ECJ or the European legislator.