The unencumbered European taxpayer
The case law of the European Court of Justice on personal taxes and the democratic legitimacy of the European Union

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"[P]lus des droits pour chacun (…) c'est moins de pouvoir pour tous"
Marcel Gauchet, *La Democratie d'une crise à l'autre*

Introduction

§1. This paper aims at clarifying some of the effects that the process of European economic and political integration has had over the way in which personal taxes are framed, regulated and collected in Europe.

The integration project enshrined in the constitutive Treaties of the European Communities could not have been achieved without a major transfer of tax powers[1] to the European Union[2] and the progressive Europeanisation of national tax systems. Although it keeps on being assumed that Member States retain sovereignty on tax matters,[3] this is factually wrong if it is meant to understand that their tax powers

[1] Indeed, the creation of a common, later single, market required redrawing economic borders, tearing down those sheltering national economic agents from competition from other Member States and erecting new ones demarcating the inside and outside of the Union. Given that tax systems play a paramount role in defining and sustaining economic boundaries, the common market could not but require transferring to the Union substantial tax powers. This was something unnoticed by most commentators, but not all, at the time the United Kingdom, Ireland and Denmark became Members. See Norman I. Miller, 'Some Tax Implications of British Entry into the Common Market", 37 *Law and Contemporary Problems*, 265-85, p. 265: "[T]he alterations in the tax structure resulting from the impending entry would in themselves be sufficient to affect almost every aspect of Britain's industrial, commercial and social life"

[2] And, as will be said, to supranational non-public or at least non-political collective decision-making processes, basically the agents operating in financial markets

[3] See for example, Andrew Moravcsik, 'In Defence of the Democratic Deficit. Reassessing Legitimacy in the European Union', 40 (2002) *Journal of Common Market Studies*, pp. 603-24, available at http://www.princeton.edu/~amoravcs/library/deficit.pdf, at p. 607: "Much is thereby excluded from the EU policy agenda. Absent concerns include taxation and the setting of fiscal priorities, social welfare provision, defence and police powers, education policy, cultural policy, non-economic civic litigation, direct cultural promotion and regulation, the funding of civilian infrastructure, and most other regulatory policies unrelated to cross-border economic activity. Certainly the EU has made modest inroads into many of these areas, but only in limited areas directly related to cross-border flows". More surprising is the confusing claims made by some tax specialists, such as Ben Terra and Peter Wattel in *European Tax Law*, London: Kluwer Law International, 1997, p. 3, such as "the further the harmonization process and, therefore, loss of national freedom of policy in the field of *indirect taxation progresses*, the more the Member States will feel the need to defend their remaining tax sovereignty, that is sovereignty in the field of *direct* taxation *(...)* Finally, we observe that a genuine *European* tax hardlu exists as such. There is no tax levied at Community level by a Community tax authority". We can find statements of national politicians galore repeating the same core idea. Among which, consider the common position of several Member States transmitted to the Laeken Convention "Contribution by Mr Peter Hain (UK), Ms Lena Hjelm-Wallen (Sweden), Ms Danuta Hübner (Poland), Mr Ivan Korcok (Slovak Republic), Mr Dick Roche (Ireland) Mr Tunne Kelam, Mr Rein Lang; member of the Convention - Mr Henrik Hololei, Mr Bobby McDonagh, Ms Ana Palacio, Mr Robert Zile, Mr Pat Carey, Mr Kenneth Kvist, Mr Urmas Reinsalu, Lord Tomlinson, Mrs Liina Tonisson; alternate member of the Convention:- "Articles III.59 and III.60 in the draft EU constitutional treaty", DOC CONV 782/03, available at http://register.consilium.eu.int/pdf/en/03/cv00/cv00782en03.pdf, where it can be read: "We believe

remain substantially unfettered by Community law. All taxes have been Europeanised; and some of the key direct and indirect powers to set them have been transferred to the supranational level of government.[4] As a result, European integration has altered not only the formal legal relationships between States and taxpayers,[5] but also the structural economic ones, something which has resulted in new structural limits to what can be taxed and how it can be taxed. Both the legal and the economic transformations haveaffected not only *ad rem*, but also personal taxes.[6] The general shift from an encompassing definition of the income tax base to the dual income tax, observable in most European countries,[7] is to be partially, even if perhaps not fully, traced back to the liberalization of capital movements entrenched by the 88/361 Directive which redefined the legal nature and substantive content of the freedom of movement of capitals in Community law.[8] Section II of this paper provides further and concrete examples which document this. But if there should be no question about *whether* European taxation has affected the power to tax of Member States, and in particular its power to frame, decide and collect personal taxes,[9] it remains to be

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that taxation questions are, both historically and in the contemporary world, of profound sensitivity and touch very directly on the relationship of the citizen to the State. One of the key components of a State's sovereignty is its capacity to fully express the preferences of its citizens on taxation, delivered through democratic control and accountability (...)We believe therefore that the right to determine taxation issues should continue to be held at national level. Unanimity on taxation matters in the Council ensures this". See also the recent statement (June 2007) of the Slovak Christian Democratic Party on tax sovereignty, where it is (wrongly) claimed "the sole authority of the Slovak Republic to decide on the personal income tax and corporate taxes", and requires the government to oppose and reject "any legally binding acts and other acts of the European Communities and European Union that might concern the harmonisation of such taxes, of their tax base, structure or system…or against any motion to set a new (European) tax". The document is available (in Slovak) at http://www.konzervativizmus.sk/article.php?1114. The official position paper of the British government concerning the negotiations of the 2007 IGC contains similar claims. The introduction by Gordon Brown, then Prime Minister, is very revealing: "The Mandate for the new amending Treaty meets these red lines. It ensures that our existing labour and social legislation remains intact; protects our common law system, police and judicial processes, as well as our tax and social security systems; and preserves our independent foreign and defence policy. In addition, the Treaty will make clear for the first time that national security remains a matter for Member States" (my italics). The text is available at http://www.fco.gov.uk/Files/kfile/CM7174_Reform_Treaty.pdf. See also the speech by then Foreign Minister David Miliband to the College of Europe 'Europe 2030: Model Power, Not Superpower' of November 15th, 2007: "Open markets, subsidiarity, better regulation and enlargement are now far more part of the conventional vocabulary of European debate than a United States of Europe, *centralised taxation* or a common industrial policy. The truth is that the EU has enlarged, remodelled and opened up. It is not and is not going to become a superstate". Available at).

[4] See Working Paper 15/08

[5] Essentially those capable of easily and speedily transforming their wealth into financial capital and thus "escape" the national tax jurisdiction.

[6] (in which the tax liability is calculated by reference to the ability to pay of the taxpayer, and not by reference to the ability to pay which can be indirectly induced from a given economic transaction).

[7] REFERENCES

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[9] To the point that national decision-making on personal taxes is now fully framed by the "European context". More than a matter of operationalising a conception of distributive justice, it is about selecting a viable system under conditions of European integration. See for example
Christian Saint-Étiene and Jacques Le Cacheux, 'Croissance équitable et concurrence fiscale', Report 56 of the Conseil d'Analyse Économique, available at http://www.cae.gouv.fr/rapports/dl/056.pdf; and more recently, Jacques Le Cacheux, 'Mondialisation, intégration européenne, concurrence fiscale : faut-il réformer la fiscalité française?', 343 (2008) *Fiscalité et revenus*, pp. 41-47.

elucidated *when* and *how* national taxes were Europeanised, *which are the political consequences* of such Europeanisation, and *how* the constitutional framework and the decision-making process on taxes can be mended to reconstitute "tax" democracy in the European Union.

§2. In this paper I sustain that the *when* and the *how* of the Europeanisation of national taxes are to be determined by means of analyzing the implications of European economic integration through the last fifty years, and in particular, by means of distinguishing different conceptions on how to structure and govern the Europeanisation of national economic, insurance and political communities. In particular, I claim that the political mediation of the Europeanisation of economic and insurance communities which prevailed during the first thirty years of integration (which I refer as the "common market approach") reinforced the structural power of States versus taxpayers rather than undermining them. This indeed facilitated the spending effort behind the development of the European *SozialRechtsstaat* in the sixties and seventies. The shift to the "single market" confirmed in the Single European Act reverted the term of the relationship between the process of Europeanisation of economic, insurance and political communities, as it resulted trusting the Europeanisation of insurance and political communities to the aggregative and unplanned effects of the exercise of economic freedoms at a supranational economic community of risks. This left largely unaffected the taxing powers of the Member States in *formal* terms, but ended up destabilizing them structurally. A complex web of political and judicial decisions empowered (some) private actors and rendered them capable of undermining the capacity of Member States to track income flows (a result of "liberalization" of the movement of capitals without administrative and tax harmonization) and to coerce taxpayers into compliance (a result of the empowerment of companies *vis-à-vis* the countries of their primary establishment without the harmonization of the corporate tax and regulatory framework).

Analysing this complex web of decisions is an engaging task which will be discharged over the five years that RECON lasts. In this paper I limit my focus of attention to the case law of the Court of Justice where national personal income taxes meet freedom of establishment and free movement of workers.[10] I further sustain that these transformations have had serious political consequences, although it must be said that the impact of the case law of the Court has varied over time. As long as the Court of Justice observed self-restraint on what concerned the soundness of national personal taxes, it clearly assumed that the democratic legitimacy of the European Union was to be ensured by the transfer of democratic legitimacy from the Member States to the Union (and thus assumed that the democratic legitimacy of personal taxes could only derive from national democratic processes). Its more "pro-active" jurisprudence from the Single European Act to the beginning of the third phase of the Monetary Union limited itself still to monitor the extent to which national tax norms discriminated against "transnational citizens", and consequently could still be reconstructed as aimed at filtering the substantively wrong outcomes of national

[10] One must start somewhere, and the judgments of the Court (and the opinions of its Advocate Generals) are a good place to do so, if only because they reflect a wealth of contradictory views on how to solve hard constitutional cases, in which it is unavoidable to reflect on what the European Union should be and why one solution is preferable and more legitimate than others; precisely the kind of questions that RECON is interested into.

decision-making resulting from the insufficient inclusiveness of national political process, i.e. to the non-representation of "transnational citizens". This implied a modest degree of constitutionalisation and juridification of the European law of personal taxation, but was still a very moderate move in a federalizing direction (compatible both with a liberist or a social-democratic understanding of the powers of the Union as a tax federation). Finally, the shift towards a transcendental understanding of the economic freedoms, detached from the contextual construction which characterizes national constitutional traditions, has led to a pervasive review of the European constitutionality of personal taxes, which pushes the Community towards the liberist federal model.

§3. The paper is structured in two parts. In the first section, I offer a reconstruction of the evolution of the socio-economic constitution of the European Union. In particular, I consider how the relationship between economic, insurance communities has evolved under the "common market" and "single market" paradigms of European integration. In the second section, I reconstruct the case law of the European Court of Justice on personal taxation against the background established in the first. I find that while its jurisprudence on turnover and other ad rem taxes basically moved along the lines of the general socio-economic constitution, its case law on personal taxation has some differentiating factors; in particular, the Single European Act moved the Court from complete self-restraint into a limited role as guarantor of the rights of "transnational citizens", overcame at the end of the century by its decisions as guardian of a transcendental European constitution. I also consider the underlying conception of the European Union and the sources of democratic legitimacy implicit in each phase of the case law of the Court of Justice, which prompts me to some preliminary remarks on how they relate to each RECON conception.

I. European integration or the complex reconfiguration of the relationship between economic, insurance and political communities.

§4. The constitutional order of Europe circa 1951 was grounded on the overlapping geographical scope of the economic, political and social insurance communities. The community of economic risks involved in the process of production and distribution of goods and services included the very same citizens who pooled in collective insurance institutions the risks derived from both their economic activities (mainly unemployment, sickness and old age) and from the fragile character of human existence (providing insurance against a variety of risks and guaranteeing social and political inclusion through redistribution of economic resources). The terms of the relationship between the community of economic risks and the community of social insurance was mediated by the political institutions through which the political community give itself the means of implementing the *volonté général*.[11] As is very well-known, law as a means of social integration was progressively tuned to this task, and indeed was transformed from a formal means of integration, basically aiming at solving conflicts, to a material means of integration, capable of progressively realising

[11] Not always that was so. See Abran De Swaan, *In Care of the State*, Oxford: Blackwell, 1988.

substantive goals which increasingly implied the coordination of the action of millions to achieve collective goods.

In this context, the tax system in general, and income taxation in particular, played a key role. The affirmation of personal income taxation as one of the five fundamental sources of revenue of modern states was key in increasing the breadth and scope of democratic decision-making, not only as it provided the financial means to fund the modern welfare state, but also because it ensured that *we the people* could take collective decisions enforcing the mutual obligations that citizens have towards each other. It is because central components of the tax system were progressive personal income taxes that the tax system as a whole could operationalise the solidaristic obligations which derive from membership into a political community.[12] Similarly, the emergence of the modern corporate income tax was motivated by serious concerns over the incidence that the rise of "corporate" capitalism had over the actual feasibility of democratic government; corporate income taxation was developed as a way to make corporations pay for the public goods and services they were provided with (including the limited liability granted by law) but also to enable democratic decision-making curbing the excessive accumulation of power in the (potentially eternal) institutional structure of the corporation, and to influence private investment and contracting decisions so as to create the conditions under which *we the people* could realistically decide how and the what extent certain collective macro goals, such as stable growth and full employment, were to be aimed at.

Or to put it differently, the progressive development of modern personal taxes provided democratic governments with the tools with the help of which they could at the same time shape the contours of the community of economic risks, ensure that a part of the total product of society was channelled to the provision of key public goods and services through which all citizens were insured against a set of economic and existential risks, and to do both things in such a way that decision-making on the socio-economic order of the polity would result in meaningful and effective decisions.

§5. European integration may well be said to have aimed at recreating the structural relationships prevailing at the national level between the communities of economic risk, social insurance and political decision-making at the supranational level. Very specific historical factors, [13] together with the sheer complexity of the task,

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[12] Indeed, the relationship between democracy and personal taxation is very close and bits both ways; the complex and protracted development of personal income taxes seems to indicate that there is a intimate association between personal income tax becoming a central element in national public finances and the consolidation of inclusive democratic political processes (indeed, a modern personal income tax can only be collected when citizens are capable of trusting each other as citizens of a democratic polity do).

[13] It is well-known that the achievement of durable peace and solid prosperity through supranational institutional structures and a supranational legal order had been the objective of generations of Europeans. After two devastating wars in twenty years, such a need was felt even more urgently.[13] Of the manifold projects launched after 1945, the European Union was the one which bore fruit; not by chance it was characterised by aiming at political union through economic integration, assuming that the basis of enduring integration could only be laid if economic borders were redrawn and enlarged. That required establishing common institutions and decision-making processes, but given the concrete strategy followed, on a scale much more modest than what would have been the case in a federal union. Economic integration was thus the path of least resistance because it did not immediately and directly challenge the central role played by nation-states in the social and political integration of Europe. It was assumed that the establishment of a common market would not only increase the number of competitors and the size of the market, facilitating the economies of scale necessary to improve

both in factual and normative terms, account for the fact that integration did not proceed by the constitution of a new and autonomous supranational political community (complete in institutional and decision-making terms), but through an open-ended process of synthetic construction of a supranational political community, firmly grounded for the time being on the institutional capabilities and legitimacy bases of national political communities.

§6. This explains why the founding Treaties of the European Communities, and very especially, the Rome Treaty establishing the European Economic Community, launched three simultaneous processes.

First, they laid down a rather concrete and detailed set of specific initiatives to be undertaken in the way to establishing the foundations of a "common market", critically including the establishment of a customs union and the consequent elimination of any tariffs, quantitative restrictions or measures having an equivalent effect in the internal relationships between Member States. The concreteness of the set of norms specifying what was to be done in each of the four stages towards the common market explains the persistence of the claim that Community law was indeed a "regulatory" order in a technical legal sense.[14] The immediate objective of the said norms was to "open up" national economic and insurance communities, allowing access on equal conditions to physical and legal persons resident in other Member States (thus creating six common markets and six common welfare structures by means of *communitarising* all national markets and welfare structures). Or what is the same, national communities of economic risk and of insurance were expanded so as to include Community nationals (and the companies established in the Communities) with the same rights as nationals.[15] Still, it must be noticed that inclusion in the insurance community remained conditioned for non-nationals on actual contribution to the national economy through the production of either goods or services.[16] Second, and next to this set of detailed rules, the TEEC set the objective of a fully integrated market by reference to a set of principles (now enumerated in Article 3) which should

productivity, but would also make possible the widespread recognition of the citizens of all other Member States as members of the same political and economic community, thus nurturing the kind of we-feelings and solidaristic predispositions characteristic of modern democratic welfare states. Or what is the same, that it will result in the transformation of the community of economic risk as a welfare community, as a result of the establishment of mechanisms of public insurance against economic risk underpinning the legitimacy of the socio-economic order. It can thus be said that the Community project drove a middle way between those blueprints which aimed at improving the intergovernmental mechanisms of the League of Nations, but left intact formal national sovereignty (i.e. the Council of Europe) and those projects which aimed at the direct and immediate establishment of a European federation (as European federalists advocated, and basically succeed in inscribing in the –failed- Military and Political Union of 1954).

[14] Indeed, most of the Treaty establishing the Coal and Steel Community looked like a long and complex statutory regulation more than a statute.

[15] Quite obviously, the structural conditions which rendered the process a manageable one were not all of them under the direct control of European political institutions. It is rather obvious that European integration would have proceeded differently had the international financial architecture been different in the fifties and sixties. Indeed, the collapse of the Breton Woods system instigated by the Nixon administration was close to provoking the collapse of the key policies of the Communities. The process of European integration was then perhaps closer than ever to collapse.

[16] (even if what was counted as a valid reason to include somebody will be extended so as to cover dependent relatives and those who did formally work; but such development was always dependent on a link to active work)

be progressively realised as integration proceeded. The long-term objective was to fully merge national economies into what (following the later terminology) could be referred as a single market, in which the line drawn between nationals and Community citizens will be deleted. Key normative elements in this regard were the famous four economic freedoms, which were partially operationalised in the programme towards the common market, but the breadth and scope of which was clearly intended to be much larger. As all principles, the norms enshrined in Article 3 aimed at progressive realisation as far as it was factually and normatively possible. This explains why the TEC was also regarded as an open-ended Treaty, contrasting in this regard with the "regulatory" Paris Treaty (and in a certain sense, the Euroatom Treaty).

Third, and last but not least, the founding Treaty of the European Economic Community rendered explicit that both the "common market" and the "single market" were not ends in themselves, but aimed at achieving the political integration of Europe (even if the process was expected to take a long time; indeed the "ever closer Union" was regarded as a frustrating avenue by federalists). The political ethos of the Treaty comes a long way to explain the insertion of grand phrases, and more specifically, the inclusion of the aims enumerated in Article 2 (recently edited and updated in the preamble to the Charter of Fundamental Rights), which must be constructed as reflecting the constitutional principles common to Member States which are especially relevant in the realisation of a complex process of political integration.

By means of aiming simultaneously to these three aims, the TEEC rendered clear that neither economic integration was a self-referential objective, nor the definition of the institutional setup of a European market could be undertaken without reference to the political objectives of the process of integration as a whole. But it left open most questions concerning how the integration of economic, insurance and political communities was to be achieved once the "communitarisation" of national markets was completed. Indeed, the process of European integration was bound to alter the relationship between the three communities (economic, insurance and political) which structure the socio-economic structure of modern societies; but in which sense and with which results was not fixed once and for all.

§7. During the "common market" stage, the democratic legitimacy of the process of integration was guaranteed by the "double" anchoring of Community law and institutions to national constitutions and decision-making process. First, the constitutional framework of the Communities was supposed to mirror the constitutional order of the Member States, being constituted as it was by a "deep constitution" consisting in the "common constitutional traditions" of the Member States and a "constitutional charter" enshrined in the founding Treaties of the Communities, which essentially rendered partially explicit what the common constitutional principles entailed for the process of integration of the economic, insurance and political communities. In particular, the four economic freedoms which were expected to underpin both the common and the single markets were constructed as entailing the expansion of the rights enjoyed by nationals within the national economic and insurance communities to other Community citizens. Second, the re-arrangement of socio-economic institutions so as to realise integration goals was foreseen to require *secondary* Community norms (i.e. regulations and directives)

spelling out in detail the normative implications of integration; but those were to be deliberated upon and decided in processes which guaranteed that the Community general will was essentially the result of aggregating national general wills, as expressed by national governments accountable at the end of the day to the direct representatives of citizens (this was in particular the case of the classical "Community method", where the Council retained the exclusive power to transform proposals into what were laws in everything but name). On such a basis, the democratic legitimacy of the Communities was either transferred from national political processes to supranational decision-making procedures via the national constitution and the national actors granted a veto right over Community decision-making; or it was grounded on Community norms and decisions limiting themselves to implement decisions collectively taken in the founding Treaties (with Community institutions acting as a kind of supranational administrative agency).

As a result, economic borders did not disappear, but were essentially reconfigured. On the one hand, they were redrawn at the Community level vis-à-vis the rest of the world, and strengthened through the use of the panoply of tax and regulatory norms through which economic borders were erected in the system of sovereign nation-states which slowly emerged at the end of the XIXth century. On the other hand, national borders were rendered sufficiently porous to enlarge the right to equality in economic and social matters to all Community nationals, but were kept sufficiently firm as to shelter the autonomy of national political decision-making process, very especially on what concerned the configuration of the socio-economic order.

As a consequence, national political institutions retained most of the key powers shaping the communities of economic risk and of insurance, although they collectively exercised a modicum of them. No area or competence was to be shifted from the "common markets" to the "single market" side of the construction without an explicit political decision; moreover, temporary waivers or exceptional measures could be agreed limiting the scope of the single market if regarded politically necessary.[17] The European Court of Justice, in cooperation with the national courts which requested preliminary judgments from it, acted as a guardian of European constitutionality, of the set of principles which framed the Community legal order (and increasingly also national legal orders as integration advanced). But its legitimacy was based on its role as defender of the rights of "transnational citizens" as Community citizens. Because such rights were deemed to emerge from Community constitutional norms which mirrored national constitutional norms, and because the Court limited its use as constitutional yardstick to the testing of national norms which placed non-nationals on a different footing than nationals, the Court could claim that it was acting in exclusive defence of the rights of those who were intensively affected by national norms, but were still excluded from democratic deliberation and decision-making processes. Indeed, European integration in general, and the constitutional role played by the European Court of Justice in particular, rendered national decision-making processes more responsive to the interests of non-national but Community citizens. The principle of non-discrimination on the basis of nationality contributed to frame the substantive exercise of national powers, rendering void national norms or decisions which discriminated against "trans-national citizens" without weighty reasons.

[17] Thus the numerous safeguards and firewalls built upon the TECSC and the TEC.

§8. The communitarisation of national markets was expected to be a transitory phase leading to further economic and political integration. Indeed, the objectives of the fourth stage of the common market, which according to schedule were to be reached on January 1st 1970, were declared fulfilled eighteen months earlier. How the key principles expected to govern the single market were to be realised in ways which will not destabilise national insurance and political communities, but will allow projecting them to the supranational level, did only have a procedural answer in the Treaties. The Council was expected to agree on *how* to do it.

This proved a tall order in the stable political and macro-economic context of the *thirty glorious years of the postwar* (as the empty chair crisis, sparked by the assignment of taxing powers to the Union, proved); and a rather impossible task after the two oil crisis of the seventies questioned some of the basic premises on which European integration was grounded. On the one hand, the postwar consensus on the imperative need of the political steering of the relationships between economic, insurance and political communities was seriously contested. While some Member States stood fast to Keynesian macroeconomic policies, others opted for "emancipating" actors in the economic sphere from political control, and in doing so narrowing the scope of insurance communities. On the other hand, the economic crisis rendered evident that the European institutional structure was not attuned to serve the purpose of collective management of the crisis. Member States reacted in uncoordinated ways which put into peril the stability of common economic policies (and consequently the *acquis communitaire*). Power was so fragmented that no actor seemed capable to actually deciding anything,[18] so that the European political order seemed bound to slowly but steadily descend into irrelevance.

This crisis, usually labelled as *Euro-sclerosis,* reinforced previous doubts about the adequacy of Community decision-making procedures. While the complex democratic legitimacy equation may have been a rather apt solution when the tasks ahead had been basically agreed in the Treaties, it was bound to paralise decision-making when it was necessary to select the proper means to realise the general principles which underpinned the single market and the political integration projects.[19]

§9. Slowly but rather firmly, a consensus emerged among European elites concerning the need of inverting the relationship between economic and political integration. In the absence of a "thick" political agreement on the way the complex relationships between economic, insurance and political communities should be governed, it was hoped that increasing the breadth and depth of integration of national communities of economic risk could relaunch integration. This seemed to offer equal promise to actors upholding rather contrasting conceptions of what the European Union should become. It was welcomed by the growing numbers of

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[18] Leaving aside some symbolic decisions of the European Court of Justice (such as the one taken in *Dassonville*.

[19] There were several concurrent explanations of why this was so. But some of them claimed that the root of the evil was indeed in the combination of unanimous decision-making in the Council before any integration decision could be approved and the subjection of economic integration to political steering. After all, both were forms by ways of which politics meddled into the self-stabilising and adjusting capacities of (European) markets.

political actors who blamed on political meddling of the relationships between economic and insurance communities the economic crisis which affected the Union, and who had been implementing an agenda which basically consisted in narrowing the community of social insurance and increasing the freedoms enjoyed by actors in markets (a double process of privatisation of communities of economic risk and of insurance). For such actors, the European Union held promise as the level of government at which the right constitutional norms setting up supranational markets could be established. At the same time, and for different reasons, pushing for further economic integration without additional Europeanisation of the insurance and political communities was regarded as a promising alternative route to achieve the ultimate reconstitution of a coherent relationship between economic, insurance and political communities at the supranational level. In particular, some of the actors upholding a federalising view of the Union came to believe that speeding up economic integration will necessarily result in strong demand for further social and political integration. For those actors, the Single European Act was indeed the kind of measure which was bound to generate the sequence of spill-overs[20] which would lead the Communities to the original destination (political Union in a social-democratic fashion) only through a different route.[21]

§10. Still, the wider objective of creating a single market was bound to disrupt the consistent overlap of economic, insurance and political communities. This was so because economic integration was really about erasing economic borders within the Union; this could not be affect the functioning of insurance and political communities, as they relied on the political power to buffer national economies through the exercise of various tax and regulatory powers. And as the structural power to draw borders was weakened, and indeed the legal and structural power of Member States acting alone to resort to functional equivalents was undermined, reliance on economic integration implied that there was no supranational political community in the making which could mediate the relation between (national) social communities and (supranational) economic communities. As a consequence, neither the states nor the weak supranational polity could really take decisions rectifying the distributive consequences of integration so as to re-establish a coherent relationship between the three communities. But if nobody could decide, there was a serious risk of affecting the very structural basis on which democratic government rested, and on which the sustainability of complex modern welfare states was dependent.[22]

§11. It is no surprise then that the democratic legitimacy of the process became less obvious as it shifted away from the "transmission belt" plus "governance" model to

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[20] This forms the core of the "spillover" mechanism, described by Ernst B. Haas, The Uniting of Europe, Political, Social and Economic Forces, Stanford: Stanford University Press, 1958. The argument of the spill-over is the background of the key Neumark report of 1962, see Rapport du Comité Fiscal et Financier, now available at http://bookshop.europa.eu/eubookshop/FileCache/PUBPDF/CB6208070FRC/CB6208070FRC_002.pdf

[21] See Delors, Memoires, and Abdelal, Capital Rules, Cambridge: Harvard University Press, 2008.

[22] It may be the case that a good deal of the unrest and growing disaffection with the project of European integration has a lot to do with the inconsistencies and subversive effects unleashed by this asymmetric process of Europeanisation of markets unconstrained by the establishment of European political and insurance communities.

an unclear destination. On the one hand, the "double" anchoring of Community law and institutions to national constitutions and decision-making process was simultaneously weakened. For one, the "propelling" role assigned to economic freedoms implied assigning them a far superior weight and a different substantive definition than they had in the common constitutional traditions of the Member States. As a result, it was increasingly difficult to regard them as mirroring national constitutional norms, and consequently, transferring their democratic legitimacy to the Community legal order. They started to be regarded (for plausible if not always sound reasons) as the Trojan constitutional horse bound to undermine national constitutions. For two, a bifurcation was made on Community decision-making processes, by means of establishing a division of labour between the "Community" method and a new hybrid process, which after some amendments would emerge as the co-decision procedure, where the European general will is defined as the aggregation of the majoritarian national will (as expressed by Member States) and the majoritarian European will (as expressed by the European Parliament. This was neither a new decantation of the "transmission belt" legitimacy, nor still a source of direct democratic legitimacy for the Union, but something in between. Additionally, the criteria according to which labour is divided between the two procedures raises serious concerns about the existence of a structural bias of the constitutional setup of the Union in favour of certain substantive outcomes, very especially on what concerns the socio-economic structure of the European political order. This explains the apparent paradoxical outcome that the more powers are granted to the European Parliament by expanding the scope of co-decision, the more the democratic legitimacy of the Union seems to be undermined.

As a result, the borders of the community of economic risks started to disappear, but this did not automatically result in the acceleration of either the process of Europeanisation of communities of economic risk, or of the creation of a supranational political community;[23] instead, it may be argued that the outcome was a transfer of substantive decision-making processes from both national and European political decision-making processes to private decision-making processes. This process of "private" empowerment was reinforced by the European Court of Justice, which has redefined in a transcendental sense the four economic freedoms, and transformed them step by step in a yardstick of constitutionality of all national norms, including those whose regulatory purpose is to mediate the "internal" relationships between economic, insurance and political communities, and not substantially to affect "transnational" citizens (even if they could have as a side and marginal effect that result).

II. The Case Law of the European Court of Justice on Personal Taxes: Elements for its Theoretical Analysis

A) Constitutional Decisions on the European Tax System: the Treaty of Paris and the Treaties of Rome

[23] It remains to be seen whether the "transcendental" understanding of the single market as a constitutional order which empowers (some) private actors and narrows down both the insurance and political communities stands a chance of stabilising itself, or on the contrary fosters a process of recreation of the insurance and political communities at the supranational level.

§12. The Treaty establishing the European Coal and Steel Community (hereafter TECSC) aimed at establishing a "common market" in coal and steel through negative and positive integration of those economic sectors.[24] The specific institutional and substantive implications of such a blueprint were rather less defined than what is usually assumed.[25]

On what concerns taxes, the Treaty affirmed in compelling terms that import or export duties among Member States were prohibited.[26] But perhaps the most interesting provisions affecting the design of national tax systems were those contained in Articles 60 to 64 of the Treaty, in which the principle of non-discriminative pricing within the common market was enshrined. In the very early days of the Community,[27] it was intensively (and angrily) discussed[28] whether "non-discrimination" in pricing implied:

A. that goods should be exported "free of national tax" (either by exempting the product or the industry from taxation in the country of origin, or by restituting the taxes paid before exportation), and then be subject to an equalising tax in the country of destination (equivalent to the taxes the goods would have bore had they been produced there); indeed the standard principle in international trade law;[29] or
B. that non discrimination on pricing excluded the combined practice of restitution and equalisation, as that could not but lead to manipulations through which actual competition could be curtailed (as it was not possible to determine in an objective manner neither the indirect nor the direct tax

[24] The Treaty which established the European Coal and Steel Community (hereafter TECSC) has been rightly characterised as a "rule-based" Treaty, made up of specific norms framing the action of the supranational administration (the High Authority) at the core of the new supranational organisation. REFERENCE. On the relationship between the positive integrative measures contemplated in the TECSC and the socio-economic model underpinning the Treaty, see Stefano Giubboni

[25] Indeed, the creation of a common market was regarded as fully compatible with the fact that the coal industry was fully nationalized in France, and so heavily regulated in Belgium as to deprive private property of much of its core meaning in Belgium. See also article 255 TEC

[26] (Article 4, whose legal and economic relevance was limited, given that most Member States did not charge any duties on coal and steel products). Italy being the exception. Special arrangements allowed Italians to keep on charging duties, although they were to be phased out at increasing speed, and to have been fully abolished by 1958 (see Article 27 of the Convention on Transitional Provisions. However, it did not mandate the full harmonisation of tariffs applicable to products from third countries, although Article 72 empowered the Council to fix minimum and maximum tariffs, and Article 74 granted the High Authority the competence to intervene if the rates at which customs duties were fixed facilitated dumping practices.On the actual practice in the first years of the ECSC, see Haas, 1958, page 103.

[27] The TECSC entered into force on 27 July 1952, and the "tax debate" was launched when the common market for coal, iron-ore and scrap was opened 13 February 1953.

[28] The background problem which originated the discussion was the differentiated pricing practices followed by German coal producers, who charged different prices at the home and at the export markets. They were forced to introduce a homogeneous price. This did not immediately guaranteed that French producers paid a similar price to that satisfied by German concerns, given that German exporters could be inclined not to deduct from the price the turnover taxes compensated at the border. The High Authority strictly forbade not to deduct compensating taxes.

[29] For the principles applied in international trade law, and in the Belgian-Luxembourgois and the Benelex communities, see J M Hostert, 'The Court of Justice of the European Communities and the Interpretation of the Tax Provisions of the Rome Treaty', 43 (1966-67) *British Yearbook of International Law*, pp. 147-176.

burden bore); consequently, imported goods would "carry" with them the taxes paid at the country of origin (and thus, the national level of taxation would be a direct part of the equation of competitiveness for each producer).

Besides the specific economic interests of those advocating one or the other position,[30] each of the two entailed a different notion of what the common market was about, and consequently, about a different understanding of what national taxes should be directly affected by Community law.

A. Option (A) was underpinned by an understanding of the common market as described in **§6,** that is, as a combination of *national common markets*, to be open to economic agents from all Member States by means of the deployment of the "negative" principle of non-discrimination to get rid of all national measures which burdened more heavily non-nationals or non-residents (*but not others*), and a *genuine single market*, to be constructed step by step through explicit political decision-making. The co-existence of the six common markets and the single market was to be critically guaranteed by the maintenance of the institutional and substantive conditions under which differentiated tax systems could be effectively maintained and reproduced, and through them, Member States will maintain a margin of discretion to take decisions if the evolution of the integration process threatened to seriously disrupt the socio-economic structure.[31] As such, option A) must be seem as the midwife (and temporary stand-in) of a federal European Community, under which market integration will come hand in hand with the harmonisation of the whole set of socio-economic regulations, including taxes, wage policies and social insurance mechanisms. But in the short run, this entailed that integration only required harmonisation of turnover taxes, of the indirect taxes which directly fell upon goods which were traded across national borders.
B. Option (B) was underlined by a rather different understanding of the common market as a single market, where competition will not be limited to production costs as such, but to all factors having an incidence in the final price. This implied either trusting in the uncoordinated adjustment of the national regulatory frameworks under the pressure bearing upon producers to outcompete the producers of other Member States, a view in line with the "ordo-liberal" views to which the German Chancellor of the Exchequer, then Prime Minister, Ludwig Erhard subscribed;[32] or in the necessity of establishing

[30] Option a) generally supported by French producers, bearing a higher turnover tax burden at home, option b) endorsed by German industries, whose turnover tax burden was lighter. See Haas, 1958, 60-61

[31] Some observers stress that this created the conditions for sheer nationalistic protectionism. See for example the very revealing editorial of the *Luxemburger Wort*, of July 9th, 1952, page 7, available at http://www.ena.lu?lang=2&doc=1125: "In spite of this, the cracks in the system are too numerous to prevent the loopholes that Governments strive to uncover in order to get around the ban against undermining competition in the coal and steel industry, and through this, to benefit their own national enterprises. The ideal arena for these manipulations is the tax system. Coal and steel manufacturers, while coming under supranational jurisdiction in production and sales, continue to be subject to taxes and national duties. The impact of this, whether directly or indirectly related to the tax burden, obviously influences the competitive capacities of the industries in question".

[32] On Erhard's "social market economy", see Anhony Nicholls, *Freedom with Responsibility: Social Market Economy in Germany, 1918-1963*, Oxford: Clarendon Press, 1994. On the relationship between

> a complete European tax system which would at the very least reduce differences between national tax systems (including personal income taxes) so as to avoid huge differences that could undermine the common market.[33]

After political and technical consultations,[34] option A) was ultimately favoured, and through it, not only a very distinct conception of what economic integration was about, but also the understanding that European integration did not concern (at least for the time being) national personal taxes. A clear-cut distinction was made between personal (income and corporate taxes) and *ad rem* taxes (turnover taxation and excises).[35] The latter (*ad rem*) were said to be generally passed to the consumer; thus, different levels of national taxation had the clear potential of affecting competitiveness within the common market, given their marginal salience in prices. The former (personal taxes) were not directly reflected in consumer prices, or at least not fully and evenly. Thus, although they obviously had an incidence over the overall competitiveness of the economic agents of each Member State, its potential impact would be mediated by the exchange rate of the national currency in the mid- and long-run, and by the companion public services funded with personal taxes.[36] This provided a rationale for the system of restitution and equalisation at the border of turnover taxation, which the High Authority added should not result in the unjust enrichment of exporters. In operational terms, adding to the market price the taxes or levies which the exporters was exempted from or restituted at the border was prohibited.[37] Moreover, the practice of restitution and equalisation at the border was intrinsically problematic given the impossibility of establishing in an objective manner the amount of taxes bearing a product in a multi-phase turnover tax system. Limiting

ordoliberalism and the economic aspects of the constitution of the European Communities, see Joerges, 'What is Left?'

[33] Having said that, it is too facile to conclude that this position was a kind of advocacy of the single market of the eighties. The relative structural affinity of national tax and welfare systems ensured that applying such a conception would not have resulted in a race to the bottom in 1953, 1957 or for that purpose 1965.[33] Still, it is clear that it would have implied favouring tax integration as a necessary but unplanned consequence of the realisation of the principle of non-discrimination on pricingSee Renner and Regul 88-97; Ernst Haas, *The Uniting of Europe*, Stanford: Stanford University Press, 1958, p. 60ff

[34] Tinbergen Report and second report commissioned by the High Authority. Rapport sur les problems poses par les taxes sur le chiffre d'affaires dans le marché commun établi par la commission d'experts instituée para la Haute Autorité, document 1057-53 of the High Authority.

[35] The distinction was first established in the Tinbergen report issued by a committee of academics, many of which were directly involved either in the negotiation of the TECSC and/or on the running of national planning authorities. REFERENCE TINBERGEN REPORT. The High Authority conveyed a committee (the so-called Tinbergen committee) which claimed that the conflict could be solved by means of adhering to the view that differences in the burden of general taxes (i.e. corporate or personal income taxes) could be compensated through the exchange rate, while differences in turnover taxes could not (as they were not unlikely to be borne by the consumer at the end of the day). This left open the question of how a levelled playing field was to be established. While it was generally agreed that any proper solution would require coherence across the board (the same system being applied in all Member States and to all products, not only coal and steel), it preferred overall a system based on compensation at the frontier limited to the amount paid in the last phase of the turnover tax. TEXT TINBERGEN REPORT

[36] On which the mixed committee insisted.

[37] Article 5 of Decision 30/1953, of May 2th, 1953, JO of 04.02.1953, p. 109. See especially Article 5: "[I]t shall be a prohibited practice within the meaning of Article 60 (1) of the Treaty to include in the price charged to the purchaser the amount of any taxes or charges in respect of which the seller is entitled to exemption or drawback".

the restitution to the last phase before exportation was a reasonable option under such circumstances;[38] but a deeper and wider harmonisation of the system of national turnover tax was called for.[39]

§13. The learning process on the effects of internal taxes unleashed by the actual implementation of the TECSC goes a long way to account for the decision to single out taxes and tax laws as a means of choice to realise the establishment of the "general" common market in the Treaty Establishing the European Economic Community (hereafter, TEC). Thus, we find in the TEC an explicit mandate to transfer substantial constitutional, legislative and collecting tax powers[40] from the Member States to the European Union.

The first stage towards the realisation of the common market was to be the creation of an economic space[41] by means of abolishing tariff[42] and non-tariff obstacles between Member States, hand in hand with the substitution of national borders for a new common economic border vis-à-vis non Member States.[43] At the heart of this

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[38] The confinement of restitution to the last phase was bound to be conflictive, precisely because French exporters were bound to get higher refunds given that France started applying VAT on April 1954 (and thus the refund of the last phase was a full refund only in the French case). On the introduction of VAT in France, see Frances M. B. Lynch, 'Funding the Modern State: The Introduction of the Value Added Tax in France', *EUI Working Paper History Department 97/2*, Florence: European University Institute. It is perhaps pertinent to stress that VAT was the final result of several innovative practices with turnover taxation, fully systematized in 1954. On the French context, see 'Options for a Definitive VAT System', *Working Paper of the European Parliament, Economic Affairs Series*, 9/1995, available at http://www.europarl.europa.eu/workingpapers/econ/pdf/e5en_en.pdf, at p. 2. More generally, see Klara K. Sullivan, *The Tax on Value Added*, New York: Columbia University Press, 1965; Richard W. Lindholm, 'The Value Added Tax: A Short Review of the Literature', 8 (1970) *Journal of Economic Literature* , pp. 1178-1189; and Allan Schenk and Oliver Oldman, *Value Added Tax, A Comparative Approach*, Cambridge: Cambridge University Press, 2007, chapter 1.

[39] This clearly illustrated the limits of "sectorial" integration and the structural "spill-over" mechanisms embedded in the very definition of the ECSC. Indeed, the obstacles stemming from the design of multi-phase turnover taxes could not be met by means of reforming turnover taxation exclusively for coal and steel, but unavoidably resulted in an encompassing reform of turnover taxation as such. On the limits of sectorial integration, see Haas, 1958, 103-110

[40] The creation of a common economic space rendered unavoidable a degree of Europeanisation of national tax systems; similarly, it made almost inescapable the transferring of some collecting tax powers to the Communities. The TEC and the EUROATOM assigned legislative tax powers to the standard Community decision-making process, thus requiring a proposal by the Commission and unanimous agreement between the national representatives in the Council of Ministers. The tax collecting powers transferred to the High Authority under the TECSC, powers framed by the text of the Treaty itself, which fixed the essential elements of the levies to be imposed. As was just said, the TEC conditioned the accrual of collecting tax powers to the Economic Community to what materially speaking was a reform of the Treaty itself.

[41] The common market was to be in full compliance with the international obligations assumed by Member States under the international trade framework. Reference Article TEC.

[42] The concept of customs union, as defined in Article XXIV of GATT, was paradigmatically defined by Jacob Viner in *The Customs Union Issue*, New York: Carnegie Endowment for Peace and London: Stevens and Sons, 1950. See also Bela A. Belassa, *Trade liberalization among industrial countries, objectives and alternatives* New York: McGraw Hill, 1967

[43] This had two main concrete implications: a) *that no customs duties could be levied on account of goods or services moving within the European Community*; this required not only the progressive abolition of such duties (Articles 9 and 13 TEC on what concerns imports, further spell out in Articles 14 and 15; and Article 16 regarding exports) but also that duties could only be decreased not increased once the Treaty entered into force (Article 12 TEC); as is well-known, Articles 30 to 36 of the TEC

endeavour was the establishment of a customs union among Member States. By definition, the customs union required the transfer of practically all substantial powers over customs duties from the Member States to the European Communities.[44] Consequently, the legislative power to actually establish the tariff duties applicable on the external borders of the Communities was to be assigned to supranational decision-making processes if the same duty was to be applicable equally and homogeneously in all Member States.[45]

But as the ECSC "tax crisis" (§12) illustrated, the objectives pursued through the customs union could only be fully realised if Member States were precluded from translating into the language of internal taxes the protectionistic devices usually operationalised through customs duties.[46] Thus, the Treaties affirmed a sweeping interdiction of discriminatory internal taxation,[47] which was immediately regarded as an "indispensable foundation of the common market".[48] On the basis of the experience of the ECSC, it was obvious that sales taxes on goods and services were the most likely means of choice to manipulate market conditions in favour of national producers and products, and thus the Treaty mandated the harmonisation of "turnover taxes, excise duties and other forms of indirect taxation" so as to realise the "interest of the common market".[49] Equalisation practices were explicitly foreseen, as an intermediate step in the "fusion" of national markets.[50]

In contrast, the Treaties did not contain but a rather limited reference to personal taxes, in concrete a mandate to conclude a multilateral treaty to avoid the double taxation of physical and legal persons.[51]

dealt with quantitative restrictions and measures having an equivalent effect. If such provisions are now regarded as the core of the principle of free movement of goods is because the customs union has been fully and successfully established; b) that a common external tariff would be established (Article 19 TEC). Article 18 TEC ensures the compatibility of the creation of the Economic Community with the international trade framework by affirming as an objective of the Community to contribute to the overall reduction of trade barriers; and Article 300X ensures compatibility with the Benelux customs union

[44] As will be seen in the next paragraphs, the fact that the duties kept on being collected by what formally speaking are national agents not only hides this transfer of power, but limits it, as the procedural norms which govern the actual process of collection of the tax are national ones.

[45] The very idea of a customs union requires the fixing of common supranational constitutional principles barring the collection of customs duties when goods or services move from one Member State to another, and pooling in common the power to fix the duties applicable to goods and services from third states. As will be seen in §, it was almost unavoidable that the transfer of constitutional and legislative tax powers will end up being accompanied by the transfer of collecting powers, as the economic dynamics unleashed will highlight the communal nature of the ensuing proceedings.

[46] Indeed, Member States have tended to claim that suspect taxes collected at the border were not customs duties or equivalent measures, but really internal taxes, and thus exempt from the prohibition laid down in the original text of the EEC Treaty by Article 9.

[47] The first two sections of Article 95 established a broad prohibition of internal taxation which discriminated against products from other Member States, while Article 96 prohibited that Member States restituted tax to exporters on excess of what they have actually paid, in order to avoid the cover subsidy of exports. Article 98 further limited such restitutions to indirect taxation, thus excluding repayments on account of corporate income tax or other forms of direct taxation)

[48] Judgment in case 57/65 Lütticke, [1966] ECR 205, p. 210.

[49] Article 99.

[50] Spaak Report, p. 13; on the need of positive and gradual action, see pp. 14-5

[51] Article 220 TEC.

§14. The definition of the general European will on tax matters as the unanimous aggregation of national general wills (as expressed by national governments) reflected both the peculiar procedure through which the European Communities were established (neither mere Treaty making nor standard constitution-making, but the *tertium genus* constitutional synthesis)[52] and the sheer complexity of decisions affecting the general structure and shape of tax systems; integration through taxation was thus not mere integration through de-taxation; or to put it differently, positive, not negative integration, was to be the main driving force in the creation of a common market through the Europeanisation of national tax systems.[53] The requirement of unanimous agreement among national governments was thus not so much reflective of deep doubts about the convenience of establishing a supranational tax system, but of the need of complex balancing and active political judgment before taking such decisions. The derivative democratic legitimacy of supranational tax norms did not prejudge the shape of decision-making rules in the future (once the system had been put into place).

B) From the Foundation of the Communities to the Single European Act: Judicial Self-Restraint

§15. From the foundation of the European Communities up to the mid seventies, tax integration was widely regarded as aiming at the establishment of a full-blown European tax system capable of discharging the same tasks that national tax systems performed in the European *SozialRechtsstaat*. Or what is the same, the European tax system was to be a system in which sizeable constitutional, legislative and collecting tax powers were exercised through European decision-making processes, so that the institutions of the Union could make use of them to provide European public goods, redistribute economic resources across borders, and contribute to the macro-economic management of the "new" continental economy. This jingled quite well with the conception of taxes as a means of social integration and macro-economic management which underpinned the tax systems of every Member State at the time of the foundation of the Communities (a conception which, as was seen, was closely related to the advocacy of a mixed economy[54] and the view of the state as a mature welfare state[55]).

The decisions taken by the High Authority of the ECSC, and very specially, the legislative proposals put forward by the Commission of the European Communities in the sixties and seventies in development of the blueprint contained in the Treaties were clearly animated by a "federal" vision of the European tax system. The studies conducted on behalf of the Commission and its specific proposals were underpinned by the view that European integration could only be sustainable if a comprehensive tax framework was agreed by the Council of Ministers and enshrined into Community regulations and directives, allowing the embedding of the emergent

[52] Reference.

[53] What was required was thus positive normative integration, not purely economic integration, or a mixture of negative integration and benign neglect leading to the undirected adjustment of national normative frameworks to the (partial) lifting and redrawing of economic borders.

[54] And very especially, the active use of macroeconomic pulls and levers to ensure stable and sustained growth resulting in full employment and a rising standard of living. KEYNES

[55] On the welfare state, DE SWANN; ESPING ANDERSEN; Rokkan, Stein. 1974. Dimensions of State Formation and Nation Building. In *The Formation of National States in Western Europe*. Ed. Charles Tilly, 562–600. Princeton, N.J.: Princeton University Press.

common market in lines along those characteristic of the embedding of national markets. This is indeed well reflected in the breadth, scope and conclusions of the very early so-called Neumark report of 1962, which comprised recommendations not only on turnover taxation but also on corporate and personal income tax.[56] The success of the Commission in implementing this blueprint was variable. A quick success was achieved on what concerned the harmonisation of customs duties.[57] Considerable achievements were secured on the harmonisation of turnover taxation; first Value Added Tax was generalised in 1967; with the decision to turn part of its yield into an own resource of the Union, additional steps were taken in harmonising the tax base and rates of VAT. Although it was far from easy to turn the widespread consensus on the desirability of moving in the French direction (i.e. the substitution of national tax systems for the "French" Value Added Tax) into specific common norms, the disagreements focused on the specific contents of the norms, the timing of

[56] In the comprehensive report, the committee constructed its mandate as a general question about the economic and political requirements for the establishment of a functional common market, upholding the (then dominant) view that markets could only operate if properly embedded in their societal context. Thus, the report defines the "common market" as requiring conditions analogous to "internal markets", which in turn requires considering factors other than the strict set of norms regulating economic activities. Firstly, the report assumes a systemic view of taxation and expenditure, highlighting the "productive" role of public expenditure, and consequently, framing in rather specific terms the tension between market integration and disparate levels of national taxation. Secondly, it affirms that the stability and efficiency of the common market cannot be ensured by mere negative integration, but requires "positive" policies, very significantly social policy. See also Segre Report of 1966. Thus, even if the committee understood the terms of reference of its report as covering the achievement of conditions similar to those of an internal market (thus including the suppression of tax borders, both physical and legal;p.7) it considered that the internal market was not merely a matter of negative freedoms, but that it could not but be underpinned by positive policies of a social and redistributive character P. 3 of the report: "Les buts économiques et sociaux poursuivis sur le plan national seraient ainsi transposes sur le plan du marché commun". And p. 12, where a uniform social and economic policy are considered to be preconditions for turning national markets into a single market. And indeed the report makes a reference back to the general objectives set in the EEC Treaty"; and in p.7 advises of the negative effect that tax discriminations would have upon the objective of establishing a common market. Third, the report stresses the need of combining an ideal blueprint of the European tax system with concrete steps through which it should be brought about, and the importance of temporary measures in the latter case, to avoid that tax integration results in serious disruption of the economic and social tissue. This explains why the report sustained the need of a profound transformation of national tax systems. Even if structurally speaking both the taxation and expenditure systems were sufficiently similar as to allow economic integration, disparities on the concrete design of specific tax figures recommended introducing major changes. The report contains clear advice in favour of the harmonisation of turnover taxation and excise duties, as well as favouring the renegotiation of bilateral double taxation conventions (that, as we already indicated, were directly covered by the provisions of the Treaty). It also calls for the prompt harmonisation of the tax treatment of cross-border capital income and of taxes bearing on the transfer of capital, as well as the coordination of the national norms governing personal and corporate income taxation, land taxes, taxes on net wealth, and even inheritance taxes and death duties. Thus, it contains arguments in favour of the adoption of a universal single income tax in all Member States, based not only on arguments of tax fairness, but also of tax transparency, judged to be essential in a common market where individuals may obtain income from economic activities taxed in different Member States (page 33).

[57] Member States agreed to a concrete calendar of reductions of internal duties, synchronised with the progressive convergence of the external tariff of Member States. Reductions proceeded in earnest, and both the elimination of tariffs within the Community and the establishment of a common external tariff had been achieved one year and a half ahead of the initial schedule, that is, by July 1st 1968. Much less substantial achievements can be registered on what concerned the Europeanisation of national customs legislation other than tariffs, besides non-binding recommendations issued by the Commission, part of which dealt with transitory norms applicable to the rolling back of national tariffs.

the reforms and the contents of the transitional norms, and so much on the desirability of establishing common norms or even on their general shape (although strong views were held- and keep on being held- on whether the EU VAT should be based on an origin or destin model).[58] But that was close to all successes the Commission could report. Not much was achieved on what concerned "personal" taxes, basically those burdening personal and corporate income. Leaving aside the directive on capital duty, the Commission did not score even one success. It did not even have much success on what concerned the network of double taxation treaties. By the time the four stages of the common market were completed, many of the pre-existing Treaties were still to be amended so as to be brought in line with the new reality of European integration, and one out of the fifteen was yet to be negotiated and ratified.[59]

§16. During the "common market stage" and up to the Single European Act, the European Court of Justice played a modest role as guardian of the European constitutionality of national tax norms. On the one hand, it affirmed itself as defender of the communitarisation of national markets by means of reviewing the constitutionality of national tax norms creating obstacles to the free movement of goods, essentially customs duties, turnover taxes and other *ad rem taxes*. In doing so, the Court relied on the central normative role assigned to free movement of goods in the founding Treaties (to this day, free movement of goods is not only the first common policy, but is regulated in a separate chapter from other economic freedoms) and on the clear-cut character of the specific provisions contained in the Treaties (very especially, old Article 9 and ff). With such arguments in hands it overcame the reluctance of national judges to even consider the review of any tax norm. On the other hand, it exerted the utmost self-restraint on what concerned national personal taxes.[60] This was partially due to the lack of incoming cases to the Court. Neither the Commission brought infringement procedures concerning national personal income

[58] As already indicated, experience from the TECSC goes a long way to explain the specific provisions on turnover taxation contained in the TEC. Its provisions affirmed both the principle of non-discrimination of internal taxation vis-à-vis the products from other Member States and the principle of capping the restitution of taxes on exportation to the amounts bore during production. The Commission put hands to work on implementing the mandate contained in Article 99 TEC, which prescribed the introduction of a turnover tax system and of restitution/equalising practices compatible with the common market. On the basis on comprehensive reports produced by committees of tax experts, the Commission tabled proposals to substitute the multi-phase taxes in force in five of the six Member States for a value added tax similar to the one applied in France since 1954. Although the tax experts had favoured "full harmonisation" (i.e. a common definition of the tax base and the setting of the same VAT rates in all Member States) as the necessary precondition for "full" market integration, the Commission opted for a rather gradualist approach. Its proposals were circumscribed to the definition of the mechanics of the new tax, leaving ample discretion to Member States on the definition of the tax bases and the tax rates. [58] Not only the proposals were not immediately acted upon, but many member states increased the amounts paid to exporters in lieu of the taxes bore during the production phase.[58] The Commission then proposed a standstill of the restitution/equalising practices, but to no avail.[58] This resulted in refocusing all efforts in the introduction of a new turnover tax. Five years after its first proposal, and scarcely two after the empty chair crisis, the first two VAT directives were approved.

[59] Ulrich Anschütz, 'Harmonization of Direct Taxes in the European Economic Community', 13 (1972) *Harvard International Law Journal*, pp. 1-52

[60] (leaving aside the personal taxes due by Eurocrats or members of the institutions to national exchequers Hublot AND OTHERS; and the case law on the Capital Duty Directive, to the extent that the latter may be regarded as a form of direct corporate taxation REFERENCES).

taxes, nor national courts posed preliminary questions concerning these issues. Still, it is not too adventurous that the Court did intentionally avoid "inviting" preliminary requests on the matter, something which it could have easily done by either offering an encompassing construction of the breadth and scope of the old Article 95 of the Treaty, or by means of *obiter dicta* which may have been interpreted as an indication of its willingness to review the European constitutionality of national personal taxes in structurally similar ways to its consideration of domestic taxes which burden in a discriminatory manner imported goods. After all, the Court made it clear in its early jurisprudence that the key provisions enshrining free movement of persons and freedom of establishment had direct effect since the completion of the fourth stage of the common market in mid 1968, exactly in the same way as free movement of goods did.[61] And still, probably under the spell of the "Tinbergen" dispute, it did not invite any exploration of whether Article 95 could be so constructed as to cover personal taxes.

§17. As a result, self-restrain left it open whether national personal tax norms were or not framed by European constitutional principles pending their harmonisation through secondary Community law, and in the eventual case that this was so, whether the European yardstick of constitutionality was to be defined by reference to the four economic freedoms, or should be constructed by reference *also* to "common national tax constitutional principles". What during all this period seemed to be accepted is that judges were not empowered to set aside national tax norms even if they entered into conflict with national constitutional provisions

§18. Self-restrain and the unwillingness to review the constitutionality of national tax norms reflected not only a certain idea of the legitimacy of the Court of Justice itself, but seems to imply that the Court endorsed the view that the democratic legitimacy of the Union could only originate in national political processes, and then be transferred to the supranational level. On the area of ad rem taxes, the Treaties did contain clear-cut decisions, which were to be implemented by the Communities as the loyal servant of the collective democratic will of the Member States. Because this was so, the Court could step in the role of guardian of the rights of transnational citizens. But on the area of personal taxes, the Treaties did not contain so clear cut-decisions, but only procedural norms which left in the hands of the Council of Ministers as a collective Community actor, or on the Member States as international actors the decisions on how to Europeanise personal taxes.

C) From the Single European Act to Monetary Union: Limited Constitutional Review to uphold the rights of "transnational" citizens

§19. The shift from the "common market" to the "single market" paradigm affected national tax systems deeply. Despite the high expectations of the Single Market programme, the successive changes of approach of the Commission (from harmonisation to the coordination of national tax systems, from positive integration to fight against harmful —but not *unharmful*— tax competition), and the successive proposals of constitutional reform of tax law-making procedures (in concrete, the move from the traditional Community method to co-decision), the transformation has

[61] REFERENCES

not been translated into changes in constitutional or ordinary Community law. Barring some limited successful initiatives on what concerns corporate income taxation (the Parent/Subsidiary Directive, the Merger Directive, and the Arbitration Convention) and personal income taxation (the Savings Directive), changes in the tax legislation have been far and between.

And still, the "single market" approach has resulted in major changes induced by the reversal of the relationship between the process of economic and political integration. In particular, legal changes determining the structural power of economic actors (very significantly, the transcendental turn in the interpretation of economic freedoms, detaching them from their discriminatory consequences; and the redefinition of free movement of capital) have seriously affected both the action of Member States as guarantors of the effectiveness of their tax systems (in both quantitative and qualitative terms) and as institutional supporters of the community of social insurance. These changes have been slowly but steadily reflected not only, and perhaps not so much, on formal changes in national tax systems (although such changes are very perceptible, it suffices to consider the number of Member States which do now collect a "flat" personal income tax, a rather improbable development only ten years ago; and the growing economic weight of VAT to the detriment of personal taxes), but in the economic implications of the same systems; the degree of realisation of constitutional tax principles has been considerably altered by the process of European integration. The concrete ways in which the four economic freedoms have been implemented has resulted in a weakening of the monitoring capacities of Member States over income flows, and consequently, in a growing gap between the *normative design* of the personal and corporate income taxes, as established in national constitutions and statutes, and the *economic distributional consequences of the collection* of both taxes.

§20. In general terms, as was already said, the shift from the common to the single market paradigm was fuelled and resulted in a distinct role of the European Court of Justice as guardian of an increasingly "transcendental" understanding of the substantive implications of Community freedoms, detached both from its previous understanding of the said freedoms as mere concretisations of the principle of non-discrimination on the basis of nationality, and of their substantive modelling mirroring national constitutional norms. But in the area of personal taxation, the shift in the case law of the Court proceeded more slowly. In the period between the Single European Act and the date at which the first wave of Member States entered the third stage of Monetary Union, Luxembourg judges carved for themselves a very limited role as guardians of the European constitutionality of national personal tax norms, by restraining themselves to the protection of the rights of transnational citizens discriminated by national norms which mainly and mostly affected them, thus upholding a definition of the breadth and scope of economic freedoms (and substantially, freedom of establishment and free movement of capital) analogous to that upheld under the "common market" approach; that is, a definition which excluded the review of the constitutionality of national norms which were mainly and mostly intended to define the overall socio-economic order, and only marginally affected transnational citizens.

§21. First came "companies" making use of the freedom to establish in another Member State through a secondary establishment, which were sheltered against

higher tax burdens stemming either from the concurrent but uncoordinated exercise of national tax powers, or simply from national tax norms which were not adapted to the reality of the common market and drew the wrong conclusions about the economic ability to pay of the companies out of the fact that they were not constituted in the national territory. Second in time, but perhaps central in terms of legal bite, came the workers who had made use of the free movement of workers recognised by Community law, and who suffered a higher total tax burden out of the concurrent claims to tax on the side of two Member States (typical at the time of entering or exiting one Member State), or as a result of the refusal of one Member State to take into account their specific personal circumstances, deriving from the "split" of their state of work and their state of residence (typical in the case of trans-border workers).
In the three leading cases[62] of *Avoir Fiscal*,[63] *Biehl,*[64] and *Schumacker*[65], the Court affirmed that the validity of all national tax norms depended on their European constitutionality, *and* that courts (led by the European Court of Justice, but also including ordinary *national* courts) were empowered to review the said European constitutionality of any national tax norm, and eventually, that national courts could and should set aside those found to be unconstitutional. This entailed the simultaneous affirmation that European constitutional norms framed national personal taxes (something which could be genuinely doubted in the first period of the case law of the Court)[66] and that judges were indeed empowered to draw the relevant legal consequences when a national tax norm enters into conflict with European constitutional norm (something was implicitly denied during the previous period). This entailed assuming that national tax powers are no longer full-blown powers of sovereign states, but competences that the Member States exercise within the framework of the European constitution, and consequently, eventually subject to a review of European constitutionality.[67]

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[62] In retrospective, it could be claimed that the Court already made some hints at the opening of a new line of jurisprudence in Case 15/81, *Gaston Schul*, [1982] ECR 1409. The latter was strictly speaking a VAT case. But in some obiter dicta, the Court actually reconstructed the scope of European constitutional norms; while until then the said principles were believed to exclusively frame "turnover" and other indirect taxes, the Court seemed to have reinterpreted them as imposing limits on national legislatures when taking decisions on any tax which could have "European" implications. See especially the opinion of Advocate General Rozès, to be found at [1982] 3 CMLR 229, at p. 236: "It had not escaped the notice of the draftsmen of the Treaty that, depending on the procedures laid down for its application, direct or indirect taxation is capable of presenting an obstacle to the achievement of the aims which they had set themselves"

[63] Case 270/83, [1986] ECR 273.

[64] Case 175/88, [1990] ECR I-1779.

[65] Case C-279/93, [1995] ECR I-225.

[66] Or perhaps, it could be doubted that the yardstick of European constitutionality of national tax norms should be mainly defined by reference to the Community's economic freedoms; and perhaps not as a "mirror" of national constitutional tax principles (which typically imposed substantive requirements of fairness to the tax system as a whole). This move was closely related to the progressive dilution in the jurisprudence of the Court of the difference (justified by the literal tenor of the Treaties) between the free movement of goods and all other economic freedoms, in its turn based on the assumption that the regulation and *materialisation* of all economic freedoms was necessary to actually uphold in an effective and fair manner the free movement of goods. Such an assumption did underpin the world economic architecture since the end of the Second World War to the late sixties.

[67] The synthetic nature of European constitutional law renders the distinction between European and national constitutional standards analytically useful but substantively confusing. The backbone of European constitutional law is indeed formed by the common constitutional norms of the Member States, partially "codified" in the founding Treaties of the Communities. On this, see my 'Sobre los

Still, the Court was very keen on restricting of the bite of European constitutional principles when reviewing national personal tax norms in ways it had not been so eager to undertake when reviewing national *ad rem* taxes. First, the Court was very careful when defining the scope of the constitutional yardsticks which determmined the soundness of national tax norms, namely freedom of establishment and free movement of workers; in particular, the Court did indeed exclude from the scope of application of the principles internal situations. Second, the Court was ready to consider "mandatory public requirements" which could justify infringements of the said freedoms, especially when it assigned a heavier weight to the general regulatory interest of the state rather than to the interests of "transnational" citizens. This led to the development of the doctrine of "coherence of the tax system" and later of the defence "combating tax avoidance", a peculiar variant of the doctrine of abuse of Community rights. This makes it plausible to uphold the decision to operate a limited constitutional review of national legislation on *democratic grounds*, if only because national law-making processes are likely to either silence or underplay the voices of those who most of the time are not even represented in them on account of their nationality (in the case of physical persons) or of their center of economic activity (in the case of corporations).

a) *The leading cases in the affirmation of a limited judicial review*

§22. *Avoir Fiscal* concerned the compatibility of tax credits granted by French law to shareholders with a view to reduce the cumulative economic effects of corporate and personal income taxes when applied to dividends. In the case at hand it was specifically discussed whether the enjoyment of the said tax credit could be conditioned to actual establishment in France (or eventually to establishment in a country –such as the Netherlands, Britain, Germany or the United Kingdom- with which France had signed a double taxation agreement which included a clause extending the right to the tax credit); or whether such requirement was in breach of freedom of establishment.[68] In its path-breaking ruling, the Court rebuffed one by one the arguments posed by the French government, and put forward two key arguments of its future case law.

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conflictos constitucionales europeos', 24 (2007) *Anuario de Filosofía del Derecho*, forthcoming. Still, the "autonomy" of the European legal order has resulted in assigning a higher weight to economic freedoms in Community law than in national legal orders. Very clearly and dramatically in the series of related judgments given which have as its "head" Case 28/67 *Molkerei Zentrale et al.,* [1968] REC 211: the most specific pronouncement can be found in the opinion of AG Gand in Case 31/67 *Stier*, [1968] REC 347, par. 3: "The Court must give a ruling on the last question asked of it, which seeks to establish whether, in so far as member-States' right to tax is recognised in principle, their rights are nevertheless subject to some restriction by reason of the Treaty as to the amount of internal taxation, and, if so, to what restrictions". A question which both the AG and the Court answered affirmatively.

[68] It is not by chance that the case concerned insurance companies. Foreign companies faced a stark choice. If they operated through secondary establishments, they were required by French law, in that respect fully in line with secondary Community law, to constitute technical reserves in France. Because they could not benefit from the said tax credit (contrary to what is the case of companies primarily established in France), they had an economic interest on sticking to bonds as a means of constituting their reserves, while companies established in France were legally authorised, and economically incentivated, to keep diversified portfolios. So foreign insurance companies not only faced a taller tax bill, but also had less room for diversifying their investments.

The key premise affirmed by the Court was that freedom of establishment (and implicitly, all economic freedoms bar from free movement of capitals, at that stage not formulated in a directly effective article of the Treaty)[69] imposed limits on the exercise of the sovereign power to tax, even if Member States had failed to agree on common tax norms at the European level:

> It must first be noted that the fact that the laws of the member-States on corporation tax have not been harmonised cannot justify the difference of treatment in this case. Although it is true that in the absence of such harmonisation, a company's tax position depends on the national law applied to it, Article 52 EEC prohibits the member-States from laying down in their laws conditions for the pursuit of activities by persons exercising their right of establishment which differ from those laid down for its own nationals.[70]

Or what is the same, the old Article 100 TEC could not be constructed as a "reserve" of power in favour of the law-maker, as an institutional rule excluding the judicial review of tax laws as long as they had not been "harmonised" by the European legislator.

Second, the Court claimed that any difference in treatment on account of nationality was to be deemed suspect, whether or not it was eventually "compensated" when considering from a systemic perspective:

> [T]he difference in treatment also cannot be justified by any advantages which branches and agencies may enjoy vis-a-vis companies and which, according to the French Government, balance out the disadvantages resulting from the failure to grant the benefit of shareholders' tax credits. Even if such advantages actually exist, they cannot justify a breach of the obligation laid down in Article 52 to accord foreign companies the same treatment in regard to shareholders' tax credits as is accorded to French companies.[71]

A similar line was followed in *Commerzbank*,[72] where the Court had to discuss whether the UK Treasury could acknowledge a tax exemption enshrined in a bilateral double taxation agreement to a German company operated in the UK through a branch but deny it the supplementary payment on account of interests due between the time the tax was wrongly collected and the moment the principal was restituted.[73]

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[69] But see how AG Léger had already dropped the exception when delivering his opinión on Schumacker, par. 21: "Thus, even in areas in which they have exclusive powers, the Member States may not adopt measures which, without justification, hamper the free movement of workers (Article 48), members of the professions (Article 52), services (Article 59) *or capital* (Article 73).

[70] Par 24 of the judgment. The Court further rejected the claim that the old Article 220 could be constructed as a norm excluding constitutional review of national tax norms in the absence of a complete set of bilateral double taxation agreements.

[71] Par. 21.

[72] Case C-330/91, [1993] ECR I-4017.

[73] See also C-264/96, *ICI*, [1998] ECR I-4711; the case concerned the subjection of the right to make deductions on account of a holding company through which a consortium exercised its right of secondary establishment to the holding company holding shares in nationally established companies. Still the Court was clear-cut in denying that constructing in accordance with Community law required that the holding of shares in companies not established in the Communities was considered.

§23. *Biehl*[74] concerned the tax consequences of leaving a Member State to establish residence in another one Member State, and of establishing oneself in a Member State at a time different from the end of the fiscal year. In particular, the law governing the Luxemburgeois personal income tax precluded taxpayers from recovering the amounts withheld in excess of their final tax liability when they changed residence during the year. The plaintiff claimed that the Luxemburgeois provision did not only deter his freedom to move as a worker, but also imposed indirect discriminatory treatment upon him as a non-national,[75] breaching his right to an equal remuneration. The Court swiftly accepted the claim, and openly stated for the first time that personal income taxes were also framed by the constitutional principles of Community law:

> The principle of equal treatment with regard to remuneration would be rendered ineffective if it could be undermined by discriminatory national provisions on income tax.[76]

§24. *Schumacker* came rather later, extending the case law of *Avoir Fiscal* and *Biehl* to a peculiar variant of "transnational" citizen, namely, that of the "frontier worker" who permanently splits his work and personal life between two countries, by means of being economically active in one Member State and having her residence in another one. This resulted in manifold mistmatches, from the eventual (even if rare) simultaneous claim of national tax authorities to double tax income, to the (more frequent) denial of the status of resident to the effects of the personal income tax. Schumacker was a Belgian national and resident who worked in Germany, where he obtained more than 90% of all his income, and where he was subject to pay income tax. Contrary to what was the case in Werner, the Court ruled in favour of Schumacker and found that he had to be treated as if he was a resident, even if he was not. In this ruling and in its follow-ups, the Court did not so much expand the substantive breadth of European constitutional principles (as it had done in *Biehl*)[77] as derived from such principles a common definition of "tax citizen" by reference to the "centre of economic activity", that being where anybody (or a family for tax purposes) earns more than 90% of their income:

> In the case of a non-resident who receives the major part of his income and almost all his family income in a Member State other than that of his residence, discrimination arises from the fact that his personal and family circumstances

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[74] Case 175/88, [1990] ECR1779. Case 24/92, *Corbiau*, [1993] ECR I-1277 dealt with the same issue, even if the preliminary request focused on whether the administrative body to which taxpayers could appeal was to be regarded as providing judicial guarantees to taxpayers. Indeed, the Commission brought Luxembourg before the ECJ on account of the failure to repeal the provisions found to be in breach of Community law and the Court decided against Luxembourg again. See Case C-151/94, [1995] ECR U-3685.

[75] Given that the number of non-nationals moving and out of Luxembourg was likely, especially in the case of the tiny Duchy, to exceed by far that of nationals in the same situation).

[76] Par 12.

[77] In par. 24 it merely rephrased the key premise of Biehl: "In view of the foregoing, the answer to be given to the first question is that Article 48 of the Treaty must be interpreted as being capable of limiting the right of a Member State to lay down conditions concerning the liability to taxation of a national of another Member State and the manner in which tax is to be levied on the income received by him within its territory, since that article does not allow a Member State, as regards the collection of direct taxes, to treat a national of another Member State employed in the territory of the first State in the exercise of his right of freedom of movement less favourably than one of its own nationals in the same situation".

are taken into account neither in the State of residence nor in the State of employment.[78]

b) Limiting the scope of economic freedom when taxes are involved; and developing new justifications

§25. This entailed a rather moderate bite of European constitutional principles over national tax norms, as it basically implied the affirmation that Community law did not aim at putting into question national collective decisions over the shape of national personal tax systems *as long as* the tax systems were not used as means of preventing companies established in any other Member State from opening shop, and as a means of treating differently taxpayers from other Member States. The same did implicitly and explicitly go for the *ancillary regulatory powers* which Member States have fleshed out to ensure actual compliance with national tax laws.

§26. Indeed, the Court made that scope clear in its "counter-leading" judgments of this period, *Daily Mail* on what concerned corporate income tax, and *Werner, Bachmann* and Gschwind (and Schumacker) on what concerned personal income tax. In all of them, the Court extricated itself from the temptation to extend the power of review of the European constitutionality of national tax norms to situations in which it would have entailed giving legal bite to European constitutional tax principles beyond "border" situations, or what is the same, in circumstances in which they were not placing obvious obstacles in the exercise of economic freedoms in the European "in between", but *within* each Member State. Or to put it otherwise, it seemed to maintain that national tax norms could only be declared unconstitutional on European grounds if they discriminated against "trans-national" citizens, not if they aimed at ensuring that all those effectively linked to the economy of the Member State were effectively taxed.[79]

§27. In *Daily Mail and General Trust*,[80] the Court emphatically affirmed that not only freedom of establishment did not prevent a Member State from determining whether the transfer of the center of management and control of a company to another Member State required (or not) the previous winding up of the company, and thus the eventual extinction and renewal of its legal personality, so that that freedom of establishment did not entitle companies to freely decide when and how to re-establish themselves. It is revealing to notice that the plaintiff in the case at hand explicitly aimed at re-establishing itself in the Netherlands with a view to avoid the capital gains tax which would be triggered once it put into effect its plan to sell all its non-essential actives. The transfer of seat would have been a purely formal one, as the

[78] Par. 38. Similarly, Case 80/94, *Wielockx*, [1998] ECR I-2493 (concerning the right to deduct from taxable income profits allocated to form a pension reserve).
[79] In Case C-1/93, *Halliburton*, [1994] ECR I-1137, the Court explicitly stated that freedom of establishment was infringed because the situation was not purely internal, as the Dutch government claimed, on the basis that the final bearer of the tax was the Dutch subsidiary of the multinational plaintiff. *A contrario*, it goes that it would have been ready to explore the implications had the factual situation been different. See especially par. 18 of the judgment.
[80] Case 81/87, [1988] ECR 5505.

company had no intention to establish real economic links with its new seat.[81] If that were to come part of the scope of freedom of establishment of Community law, then not only "transnational" citizens will be empowered vis-à-vis national political actors (including not only those who wanted to enter the national economy, but also those who may want to exit it, either partially or fully),[82] but also all "corporate" actors.[83] At the same time, it advocated that the freedom of establishment stopped there. Not only the Court reminded us of the fact that "unlike natural persons, companies are creatures of the law" and that this (at least for the time being, as indeed it keeps on being the case) entailed that companies were creatures of national law" (par. 19); but its systematic interpretation of Community law implied that no further substantive contents could be drawn from freedom of establishment as an economic freedom, and that the further specification of the issues at stake depended on the democratic exercise of European decision-making:

> It must therefore be held that the Treaty regards the differences in national legislation concerning the required connecting factor and the question whether--and if so how--the registered office or real head office of a company incorporated under national law may be transferred from one member-State to another as problems which are not resolved by the rules concerning the right of establishment but must be dealt with by future legislation or conventions (par. 23).

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§28. In Werner,[84] the Court rejected that Community law governed the relationships between German tax authorities and a German national who earned all his income in Germany through a dental practice, but who was resident in the Netherlands. By claiming that there were "far-reaching differences"[85] between the two cases, and that the German citizen remained subject to German law,[86] the Court made it clear that it did not consider Werner as a "trans-national" citizen. The rationale of this distinction was perhaps more clearly stated in *Schumacker*, when the Court borrowed the key distinction of international tax law between the treatment that residents and non-residents deserve:

> In relation to direct taxes, the situations of residents and of non-residents are not, as a rule, comparable (…) Consequently, the fact that a Member State does not grant to a non-resident certain tax benefits which it grants to a resident is not, as a rule, discriminatory since those two categories of taxpayer are not in a comparable situation (par. 31 and 34).[87]

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[81] See especially pars. 37 and 38 of the ruling. AG Darmon insisted on the relevance of effective economic links when claiming the right of freedom of establishment: "[Freedom of establishment] always implies a genuine economic link", in [1988] 3 CMLR 713, at p. 717.

[82] In the case of Daily Mail, the Court made it clear that the right to establishment rules out that the country of establishment hinders the development of economic activity in other Member States; see par. 16 of the judgment.

[83] As we will see in §, each scenario entails very different consequences.

[84] Case 112/91, [1993] ECR I-429. Whether compatible with the "inturn" turn of the citizenship jurisprudence.

[85] Par 12.

[86] Par 14.

[87] And similarly in Case C-336/96, *Gilly*, [1998] ECR I-2823 and in Case C-391/97 *Gschwind* [1999] ECR I-5453.

Indeed, if Mr Asscher was found to be in a comparable situation to residents even if he was not so, and did not obtain most of his income in the Member States whose legislation he regarded as discriminatory, was because the Dutch law calculated the tax base of residents and non-residents in exactly the same way. The defence of the progressiveness of the Dutch tax system did not require leviying a higher tax on "foreigners", but merely including foreign income for the purpose of calculating the applicable rate; and there was no "coherence" involved when the higher tax rate was supposed to be "coherent" with a benefit granted by Community law itself (in the case at hand, subjection to the social security contributions of the country of residence and not that where the taxpayer worked part of the time).[88]

§29. *Bachmann*[89] concerned both the right of taxpayers as individuals to deduct insurance premiums when assessing their income tax liabilities and the right of insurance companies as entrepreneurs to provide their services all through the Community.[90] Mr Bachmann and the Commission contested the European constitutionality of Belgian tax norms governing the deductibility of certain premiums (relating to insurance against a variety of risks, including sickness and old-age). In concrete, the plaintiffs argued that the contested Belgian tax provisions were in breach of both free movement of workers and freedom of establishment, because they subjected deductibility to the conditions that premiums *were paid in Belgium*. And this for two reasons. First, it was more than probable that the cohort of taxpayers denied the right to deduct insurance premiums will be mostly formed by nationals of other Member States (who would have already contracted insurance before moving into Belgium); and that even if some Belgians will also be denied benefits, they were likely to suffer less economic damage than non-nationals (as they were likely to return to Belgium, and thus receive the benefits free of Belgian taxes). Thus, the contested norm posed "inconvenients" which were likely to have some marginal deterring effect on prospective "movers", and for sure entailed a less beneficial treatment for those who had actually moved into Belgium having previously contracted insurance in another Member State. [91] This was said to be enough as to ground the claim that the right to free movement of persons was been unobserved. Second, the Belgian tax provision placed insurance companies not established in Belgium in a less competitive position than that enjoyed by companies established in the country; rational taxpayers would add the "lost" tax deductions to the cost of the premium when deciding which policy to subscribe.

Both the Advocate General and the Court were persuaded by the arguments made by the plaintiffs and declared that indeed the contested Belgian provisions infringed the economic liberties of the plaintiffs. Nonetheless, and to the surprise of many, they did not believe that this was the end of the argument. Indeed, they ended

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[88] Case C-107/94, *Asscher*, [1996] ECR I-3089.

[89] Joined Cases C-204/90, *Bachmann*, and C-300/90, *Belgium*, [1992] ECR I-249.

[90] And although it was not explicitly said in the judgment, the ruling had potential far-reaching implications for the public finances of Belgium, and some other Member States (especially Italy and Greece) with high levels of public debt, by then still (partially). By the time the case was brought before the Court of Justice, the said States still imposed on the insurance companies established in their territory the obligation to subscribe public debt as part and parcel of their safe assets and reserves.

[91] As either the prospective mover had to accept the eventual cost of not being able to deduct his contributions, or the economic cost of cancelling her policy every time she moved.

up finding that the norm was a necessary, adequate and proportional means to ensure the "coherence of the [Belgian] tax system". By this it seems that it was essentially meant that the European constitutionality of national tax norms cannot not be established in isolation; but had to consider in a systemic way all the norms which assess the economic ability to pay which derives from a given economic operation (in the case at hand, all the norms applicable to the taxation of the insurance contract over the whole life of the contract, from its signature to its "maturity"). This was especially so given the fact that there is no overarching Community framework governing the interactions of Community tax systems, and this entails that each system could opt for different (but eventually equivalent, at the very least, compatible solutions with Community law).

In case at hand, this entailed assessing the relation between the rules governing the deduction of premiums and the taxation of the benefits when the contract reached maturity.[92] In particular, whether national norms could be justified as means of ensuring the coherence of the national tax system was to be determined by assessing whether the differentiated regimes applicable to "nationals" and "transnationals" were nonetheless equivalent in economic terms (or what is the same, whether the overall economic implications of the rights and duties imposed upon "national" and "transnational" citizens were equivalent).[93] The Court concluded that this was indeed the case with the Belgian tax system. On the one hand, taxpayers who subscribed a policy with an insurance company established in Belgium were entitled to deduct premiums every year in from their tax liabilities; but were also required to pay income tax on the benefits they eventually received. On the other hand, taxpayers who subscribed a policy with an insurance company which was not established in Belgium could not deduct premiums, but were not required to pay any Belgian tax when receiving the benefits. Both systems were different, but equivalent. If "transnational" citizens would be entitled to both a deduction and not to pay taxes to the Belgian states upon receiving the benefits, this will destabilize the Belgian tax system.

Without denying the explicit relevance of other factors in getting to the final decision,[94] it is plausible to reconstruct the ruling in light of the institutional and democratic implications of the different decisions in the case. In particular, what clearly distinguishes *Bachmann* from *Biehl* or *Schumacker* is that the number of national norms the validity of which was at stake was much larger in the former case. Although both the request for a preliminary ruling and the infringement proceedings of the Commission originated in "transnational" citizens who were far from happy with suffering what they regarded as a discrimination with negative economic effects, the circle of those affected had the Belgian tax norm been quashed by the European Court of Justice would have been much larger. Indeed, it is not far-fetched to claim that "national" citizens would have been affected mostly, both in numbers and in depth. Had a norm as the Belgian one been declared unconstitutional, and the right to deduct extended to premiums paid to non-established insurers, more and more "national" citizens would have considered subscribing such kind of policy. In the

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93 Second, whether the financial sustainability of national public finances would be imperiled unless the discriminating measure was regarded as justified.

94 Indeed, the rather underdeveloped stage of Community law on what regarded the provision of insurance services, or the looming implications that a different result would have had for the sustainability of Belgian public debt (and with it, the prospects of a central Member State being part of the eventual third stage of the Monetary Union).

short run, this would have required the Belgian state to reconsider overnight how to fund a sizeable part of its public debt, funded until then in part by insurance companies, obliged to invest part of its reserves in the acquisition of public debt. In the long run, it may have created structural pressures to alter the general framework of the taxation of pensions, especially if a sizeable number of "nationals" would decide to transfer their residence upon retirement, for which they would have an extra incentive: to avoid being taxed by tax authorities who had acknowledged them the right to deduct the premiums.[95]

§30. In *Futura and Singer,* the Court had to determine whether Luxembourgeois provisions subjecting the right of permanent establishments of companies established in another Member to carry forward losses to the condition that they kept accounts conforming to the accounting standards of Luxembourg, and not granting it when they were kept according to (in the case at hand) French standards. While the rule was regarded as an obstacle to "secondary" freedom of establishment, the Court emphasizes that "the effectiveness of fiscal supervision was an overriding requirement" that justified limiting the said economic freedom.

> The Court has repeatedly held that the effectiveness of fiscal supervision constitutes an overriding requirement of general interest capable of justifying a restriction on the exercise of fundamental freedoms guaranteed by the Treaty (see, for example, the judgment in Case 120/78 REWE-Zentral (`Cassis de Dijon') [1979] ECR 649, paragraph 8). A Member State may therefore apply measures which enable the amount of both the income taxable in that State and of the losses which can be carried forward there to be ascertained clearly and precisely (…) As Community law stands at present and contrary to the Commission's submission, the aims pursued by the second condition would not be attained if, in order to ascertain the constituent amounts of the basis of assessment, the Luxembourg authorities had to refer to accounts kept by the non-resident taxpayer pursuant to another Member State's rules (….) As yet, no

[95] A good deal of the ensuing confusion with the notion of "coherence of the tax system" may derive from the fact that the Court wished two strike two objectives simultaneously: to retain the larger breadth and scope of economic freedoms, now "capturing" in their constitutional next national tax norms; and to avoid erecting itself in a constitutional judge of national tax norms. While in *Daily Mail* it opted from excluding from the very definition of freedom of establishment the legal prerogative to change the seat of the company without being forced to wind the company up, thus avoiding expanding the breadth and scope of freedom of establishment beyond the situations in which companies actually extended their economic activity across borders, it avoided affirming that the Belgian national tax law actually did comply with Community law. It could have done so claiming that while the tax treatment of transnational citizens was not exactly the same as that of purely "national" citizens who had never exercised their rights to free movement, or had done so without relevant economic consequences, the two regimes were equivalent. Had the Court done so, it would have to revise its blank rejection of similar claims made by national governments in previous and later cases (and even by some Advocates General).
Still, the implications of an eventual ruling declaring that the Belgian tax provision was unconstitutional in a European sense would have had consequences not only and not mainly for transnational citizens (putting an end to what seemed to be negative economic consequences for them amounting to a minor discrimination)[95] but basically for the whole structure of the insurance business in the Union. While both the Advocate General and the Court were keen also found the measure to be in breach of the freedom to provide services). But in that regard both the Advocate General and the Court clearly felt

> provision has been made for harmonizing domestic rules relating to determination of the basis of assessment to direct taxes. Consequently, each Member State draws up its own rules governing the determination of profits, income, expenditure, deductions and exemptions as well as the amounts in respect of each of them which may be included in the calculation of taxable income or of losses which may be carried forward.

In *Safir*,[96] the factual circumstances of which were rather similar to that in Bachamnn (concerning the personal income tax due on premiums paid to insurance companies not established in Sweden) the Court seemed willing to accept in principle a similar justification (by means of referring to a "tax vacuum", but found the Swedish measure a trifle unsophisticated. The Court went a long way to put forward an explicit legislative alternative:

> Other systems which are more transparent and are also capable of filling the fiscal vacuum referred to by the Swedish Government, whilst being less restrictive of the freedom to provide services, are conceivable, in particular a system for charging tax on the yield on life assurance capital, calculated according to a standard method and applicable in the same way to all insurance policies, whether taken out with companies established in the Member State concerned or with companies established in another Member State.

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§31. The combined effect of the limited scope of review of constitutionality, and the emphasis placed by the Court on the "overriding public requirements" which could serve as justifications of infringements of economic freedoms entail that the case law of the Court in this period can be interpreted as a means of correcting the persistent democratic mismatch which comes hand in hand with the creation of a single market in which tax liability remains to be determined by each Member State; and thus, while the economic community is European, and the political community is national, an increasing number of citizens experiment in economic and existential terms plural appartenance, which has to be artificially fragmented to fit into Member States.

[96] C-118/96, [1998] ECR I-1897.