



The Purse of the Polity ***Tax power in the European Union***

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Abstract

This paper describes the actual constitutional, legislative and collecting tax powers in the hands of the Union. It proceeds first to unpack the very idea of tax power, and to distinguish its elements. On such a basis, I proceed to consider European norms and practices, and to reconstruct on such a basis the tax powers of the Union. It is then found that the Union's tax powers are far wider than commonly asserted, especially on what concerns to the influence exerted on national and regional taxing powers by the Union's constitutional and legislative tax powers. However, the Union still presents most of the features characteristic of a regulatory entity. Having said that, a dynamic reconstruction of these same powers indicates that the Union is moving towards a rights-based polity, also on what concerns its taxing powers. There are clear indications that the *problem-solving* conception of the Union is insufficient to explain and ground the powers to tax in the hands of the Union.

The economic basis for the creation and preservation of democracy is the distribution of wealth and income among the majority of the people in such a fashion that no elite can permanently dominate the community.

Ratner (1967: 22)

I. Introduction

The power to tax entails the power to create and consolidate political communities. Solid civic ties between the members of a political community can only be forged and renewed with the help of the power to tax. It creates the financial basis of the provision of public goods and services to all citizens, and enables the redistribution of economic resources. In this sense, taxes are not only the price of civilization, but the very sinews of liberty and community. The power to tax is, indeed, the first and strongest component of the financial powers of any political community.¹ Neo-liberals ignore that the lack of normative legitimacy is likely to lead to an actual loss of *social legitimacy*, to social discontent and, eventually, to unrest and violence (Rawls 1971; Ackerman 1980; Holmes and Sunstein 1999; Murphy and Nagel 2002). Indeed, both the provision of essential public services and the guarantee of a certain degree of economic equality among citizens are essential in order to ensure the stability of a political community. In modern, post-industrial societies, individuals deprived of a fair access to essential public services and of public insurance against unemployment, sickness, old age and bad luck will, sooner or later, come to the conclusion that the political and legal order is tilted in favour of the powerful few to the detriment of the many. The tax system plays an essential political role, by means of operationalizing what citizens owe to each other, and by establishing legal and administrative procedures to ensure compliance with such obligations (Menéndez 2001). It is thus necessary to have a close look at the tax powers of the European Union in order to understand what kind of entity it is.

This chapter is organized in five sections. The aim of the first section is to unpack the very concept of the power to tax by reference to a general theory of democratic taxation. This allows for a separation of the different aspects of the concept, necessary for an analysis of the division of tax powers among institutions and levels of government. The second section lays down the basic conceptual framework upon which the rest of the chapter is built. In general terms, there are three basic ways of characterizing the European Union: as a problem-solving entity, as a community of cultural or pre-political values, or as a rights-based community (cf. Chapter 1). On such a basis, I reconstruct the central discourses on the power to tax of the European Union, relating both to the theoretical framework and to the empirically prevalent characterizations of the EU taxing powers. In the third section, I describe the actual tax powers of the EU. Contrary to what is usually assumed, the Union has substantive powers to tax, although not controlling a substantive tax yield of its own: The Union has constitutional and legislative tax powers which exert a major influence upon the power to tax of the member states and its regions. In the fourth section, I claim that the

¹ A distinction is made between the power to tax and the power to spend. For an analysis of the budgetary powers of the EU, see Menéndez 2004.

analysis of the taxing powers of the Union disproves the claim that characterizes the Union as a community of values, and that a dynamic reading of such powers points, although ambiguously, to the characterization of the Union as a rights-based community. The actual content and consequences of the transfers of Union tax powers underpin the hypothesis that the Union is in transition from a problem-solving organization to a political community. The last part holds the conclusion.

II. Unpacking the power to tax

Any analysis of the power to tax *of* (and *in*) the EU requires a conceptual framework which allows us to separate the different aspects of the power to tax -- the components into which it can be divided, and thus shared among different levels of government.

Traditional tax law dogmatics and classical state theory are not very helpful in this regard. Firstly, they have a propensity to present tax power as an unlimited prerogative of the sovereign.² This is reflected in the implicit affirmation that the justification of the power to tax is the very existence of the state, and in the tendency to focus on the study of concrete tax figures, downplaying the systematic aspects of taxation, at which the connection between the power to tax and political and social citizenship becomes clearer. Secondly, the power to tax tends to be aggregated rather than disaggregated. The very close connection between the state and tax power prevents distinguishing properly between the different aspects of taxing powers, and consequently neglects power-sharing arrangements among different institutions and levels of government. Indeed, the division of tax powers between the organs of the state is part and parcel of the standard operationalization of the democratic principle. Budgetary processes are typically characterized by the assignment of wide powers of initiative to the executive while the last word is reserved to the parliamentary assembly. Moreover, a monolithic understanding of the power to tax is clearly inapt when dealing with democratic states which are organized along quasi-federal lines, and thus characterized by a division of powers, including tax powers, not only among institutions, but also among different levels of government.

An alternative theoretical and conceptual framework would have to be provided by a general theory of democratic tax law, integrating insights from legal theory, normative political theory, the public finance literature on fiscal federalism (Musgrave 1965, 1969), and, last but not least, political science studies on federal polities, including the EU (Lindberg 1970; Wright 1957). But for our present purposes, it may suffice to consider three of the elements of such a general democratic tax theory.

First, in procedural terms, democratic taxes are characterized by being decided by citizens themselves (in Kantian fashion, citizens are expected to tax themselves). This general and abstract idea triggers the more concrete one of the different aspects of the power to tax. A first distinction must be made between the *normative design* of tax systems and the

² Although there are many exceptions. See Menéndez (2001: 191ff) for the three main strategies of justification followed by tax law dogmatics: procedural, substantive and through guaranteed implementation of the tax system.

effective power to apply the general norms which define them to *specific cases* -- between defining taxes and collecting taxes. The very idea of the tax system as a formula which quantifies our obligations towards others requires a general and abstract definition of each tax figure, which is later to be applied to concrete cases by citizens themselves, under the monitoring and subsidiary enforcing powers of the tax administration. At any rate, the action of the tax administration should be fully determined by the normative tax framework. This is, as is well known, an idea central to the rule of law. A second distinction concerns the different aspects of the normative tax power. In line with general democratic constitutional theory, one should distinguish between the *constitutional*, the *statutory*, and the *regulatory* normative powers to tax. At the constitutional level, citizens define the general *procedural* and *substantive* principles according to which taxes should be collected. These include the principle of legality of taxation and the principle of *non-retroactivity of taxation*. At the statutory level, citizens' representatives define the essential elements defining each tax figure, the tax base, the tax rate and the elements defining when the tax obligation is due. The *regulatory level* comprises all questions of detail, which are decided by executive powers on the basis of the general framework defined by the legislature. The key distinction is perhaps the one between the *statutory* and the *regulatory* powers to tax. Trusting too much to the *regulatory work* of the executive would imperil the democratic character of tax law, but *deciding too much* at the statutory level would deprive the legislature of the time and energy needed to legislate on other issues (Menéndez 2001: 308).

Second, the characterization of the tax system as a complex formula which operationalizes what citizens owe to each other is indicative of the close connection between taxes and conceptions of distributive justice. The assessment of tax systems requires distinguishing three main possible conceptions of distributive tax justice: the *liberist* or libertarian (which equates taxes with the prices of public goods), the *republican* (which equates taxes with the sacrifice due to fellow citizens) and the *liberal or social-democratic* one, which considers that taxes are better conceptualized as a combination of *prices of public goods* and *public insurance premiums* (see further Menéndez 2001: 149ff). According to *liberists*, taxes are a device to split the costs of the provision of public services among citizens, and taxes should be distributed according to the principle of commutative justice, because they quantify the benefit we derive from the functioning of public institutions. This could make us wonder why taxes are at all necessary, and whether the costs of public goods and services could not be met with the help of the market-price system. However, the features which define pure or quasi-pure public goods render it impossible to allocate their costs through market prices. Taxes which aim at redistribution of economic resources among citizens are to be avoided. In contrast, *republicans* regard taxes as the institutionalization of the sacrifices we have to make in favour of our co-citizens. The sharing of pre-political or cultural values creates a basic resemblance between citizens, and renders possible a degree of empathy necessary to ensure solidaristic predispositions. According to *social-democrats*, taxes represent both the best possible criterion for the allocation of the prices of public services³ and as a public insurance premium. The legitimacy of the political order is crucially dependent on the legitimacy of the basic ethical choices which underlie the socio-economic

³ The main difference with liberists being the very definition of what is to count as a public good.

order. If the order chosen is one in which economic resources are allocated through a system of private property rights, in which economic exchange takes place according to market rules, legitimacy requires a system of mutual insurance against economic risks, to be funded through a redistributive tax system.

Third, the division of powers among different levels of government in federal political communities should be arranged in such a manner as to ensure the political character of decision-making in each level of government. This entails that, in general, the level of expenditure undertaken at each level of government should be matched by a roughly similar set of taxing powers in its *legislative, regulatory and collecting* dimensions. Thus, the principle of *no taxation without representation* should be coupled with the principle of *no representation without taxation*. But how to conceive of the EU as a taxing polity?

III. The Theoretical Models

In order to spell out different policy options I rely on the reconstruction of three ideal types of the EU as a polity outlined in Chapter 1. That is, the regulatory or problem-solving entity, the value-based or communitarian, and the rights-based conception of the European Union. But I am also sensitive to actual discourses on the justification and extent of the tax powers of the Union, something which requires distinguishing two different variants of the *communitarian* conception of the EU.

A) The problem-solving conception

The *problem-solving* conceptualization of the European Union characterizes it as a functional organization and, more specifically, as a *functional international organization*, created to address pragmatic problems which they could not resolve acting independently. Institutionalization, and the consequential appearance of the Union to be a kind of *polity in the making*, would have been prompted by the need of rendering credible the commitment to common rules. This *description* is shared by intergovernmentalists, neo-functionalists and regulatory accounts of the Union (Moravcsik 1993, 1998; Haas 1958; Schmitter 2003; Majone 1996a). What differentiates them is their analysis of the *causal mechanisms* behind integration and the *normative* basis of the process. Thus, intergovernmentalists and regulatory variants of the problem-solving conception of the EU would claim that member states are the main agents of integration, and that the Union is justified by serving the interests of its member states. The legitimacy of EU institutions and legal norms would be either derivative from the member states or based on *performance* -- output legitimacy (Scharpf 1999a; Moravcsik 2003).

This characterization of the Union has clear and direct consequences for which tax powers would be *justifiable* to transfer to the Union, namely only those required by the general problem-solving tasks of the Union, and those required to solve specific tax problems accruing in the relations between member states.

The breadth and scope of the tax powers granted to the Union is related to the powers needed to create a *common market* first, and a *single market* later, between the members of the Union. Ex hypothesi, massive welfare gains are to be derived from the integration of markets of goods (and to different degrees, of labour, services and capital). Economic integration requires first and foremost the abolishment of import tax and of domestic taxes which discriminate against imported goods. This implies a close connection between the functional objective of creating a common market and the transfer of certain tax powers to the federal or supra-national level, basically of (i) negative constitutional tax powers (the prohibition of customs duties, the prohibition of national taxation which discriminated exclusively on the basis of nationality) and (ii) positive legislative tax powers (to determine the tax base and tax rates of external customs duties first, and of sales or turnover taxes later). Further transfer of tax powers is to be expected once integrating states agree on tackling additional common problems through the institutional structure of the organization they have constituted. This would explain the accrual of further, even if limited, legislative powers over corporate income taxation, personal income taxation or excises, closely related to the completion or perfecting of a *single market*. Additionally, the very implementation of the economic freedoms which are essential to the establishment of the single market create the conditions under which the effective power to tax of member states and regions might be factually eroded. This creates a new problem which can only be solved by means of establishing framework rules, and which requires the assignment of further powers to the supranational institutions, mainly on what concerns the flow of information between tax authorities and the extent to which national tax authorities must act in defence of the revenue interest of other member states.

In negative terms, the problem-solving conception predicts that the Union will not be assigned any general *collecting* taxing powers. Problem-solving conceptions would thus consider that the European budget is strictly speaking a matter of justice between member states, and not between individuals. The costs of the policies implemented at the Union level will be met by the member states, and while the budget of the Union will be larger than that of a typical international organization, this only reflects the firm will of member states to render credible their commitment to problem-solving through common institutions. This entails that the taxing powers of the Union would not necessarily be exerted according to a coherent tax distributive justice conception, but merely in order to *solve* the specific problems which member states agree to decide at the European level. This is so either because the very idea of a tax system is considered as a reconstructive device and not as a regulative ideal to be imposed upon the congeries of norms through general tax principles (as liberists will claim), or because such a task should be left in the hands of the nation-states, which would have the competence to *systematize* taxes by means of adapting the regulatory ideal to the need of common problem-solving at the European level. As long as the Union remains a tax-problem-solving organization, the conception of tax justice prevailing in the inter-state relationships will be a *liberist* one, grounded on principles of commutative justice.

On what concerns the appropriate procedure of decision-making on the functional powers assigned to the Union, the problem-solving conception clearly favours a procedure which is as *intergovernmental* as possible, with national governments in the Council having the last

word on tax matters. In the absence of a political decision-making process at the European level, only unanimous intergovernmental decision-making can ensure an *indirect democratic legitimacy* to these decisions.

The *derivative legitimacy* of the Union implies that the limited tax powers granted to the Union should be circumscribed to taxes which pursue *regulatory*, not *redistributive* purposes. This is so because redistribution is an overtly *political task* which can only be properly undertaken by a community which has direct and transparent political legitimation.⁴ This is not the case, either for the time being, or indefinitely, if the Union is merely a problem-solving regulatory regime. The limited tax powers of the Union cannot be authorized by a sufficiently legitimate decision-making process, if only because the Union is not, strictly speaking, a full-blown political community.

B) The Communitarian conception

The *communitarian* conceptualization of the European Union characterizes it as a community based on a set of ethical values, shared by all European citizens on account of pre-political factors and predispositions, typically a common culture (Benda 1993; cf. Weiler 2003). According to communitarians being a citizen is not a mere act of will, but something which is rendered possible by the pre-politically sharing of ‘something’ (i.e. a ‘culture’); turning individuals into next of kin predisposed make sacrifices for others. A pre-political we-feeling ties citizens to the political community as a whole and consequently to all its members, and renders them ready to assume their duties, because they all belong to the political unity that transcends into unity the singleness of each individual.

Such an ideal type of the Union as a political community leads to two contrasting judgments on the actual political character of the Union, and very clearly, on the tax powers which should be in the hands of the Union.

The first one is the *Euro-nationalist* variant, which leads to the characterization of the EU as a super-nation-state, to which Europeans should show allegiance; eventually, they should shift their ultimate loyalty to the Union. However, such a characterization of the Union rarely underpins actual discourses on the European power to tax.⁵ If this position becomes the one advocated by political and social movements, it will lead them to defend the transfer of a good deal of the constitutional and legislative powers to tax from member states and regions to the European Union. This would be so because the common *nationality* shared by Europeans would have to be translated into the shifting of redistributive policies to the European level.

⁴ Thus, Majone (1993: 160) claims to distinguish clearly between social regulation and social policy, the latter being focused on redistribution, and being properly beyond the reach of the Union for both normative and prudential reasons: ‘It is fortunate that the normative case for a European welfare state is not compelling, for the practical prospects are extremely poor.’

⁵ Except possibly for discussions on the need to further harmonize *sin taxes* (on alcohol and cigarettes), which are very closely related to the ethical conceptions of a community.

The second variant is the *Euro-sceptic* one, according to which the European Union cannot become a political community (in a communitarian sense) in the foreseeable future. Europeans do not share the pre-political elements which forge a community, and for such pre-political commonality to emerge will require a long process which cannot be manufactured or controlled. There is no common history or language that Europeans share (the most extreme versions claim that there is no common ethnicity). Under such conditions, Europe cannot be regarded as a political community, as a *common political will* cannot be formed (thus, the so-called *no demos thesis*) and the pre-conditions for Europeans sacrificing for co-Europeans cannot be met. It is a Union of ‘deep diversity’ (Fossum 2004). Despite the fact that the present institutional and legal reality of the Union actually contradicts the basic claims of *Euro-sceptics*, this conception underlies influential discourses on European tax powers. Communitarian Euro-sceptics consistently oppose the granting of any substantive tax powers to the Union, and would claim that, not being a political community at all, its functions should be limited to being an institutionalized forum in which member states could co-operate and exchange information and best practices. This is typically the case with British euro-sceptic arguments against harmonization, a paradigmatic example of which is the recent pamphlet by Theresa Villiers (2001).

C) The rights-based conception

The cosmopolitan conceptualization of the European Union characterizes it as a building block in the process of global institution-building. The Union would occupy an intermediate position between the United Nations and nation-states as a regional political community, based on the mutual acknowledgment of rights needed for the establishment of decision-making processes in which all those affected have the right to participate. As such, the European Union should be regarded as a *political community* part of a cosmopolitan order (cp. Eriksen 2004). Even if originally created as an international organization, its purpose clearly transcends those typically assigned to intergovernmental organizations. It has a full-blown institutional structure and a legal system into which national legal systems have increasingly fused, something which explains the *primacy* of European over national and regional laws. Decisions taken at the European level widely affect the citizens, something which requires that the democratic legitimacy of the Union be based on the democratic credentials of its decision-making procedures and the protection of the fundamental rights of European citizens.

A rights-based European Union would have wide constitutional, legislative and collecting tax powers aimed at creating the financial basis with which the Union could ensure the protection of the values of dignity, freedom, equality and solidarity. These are at the very foundational basis of the Union, as a complex political community, as reflected in the Charter of Fundamental Rights of the European Union.

The Union would be expected to acquire the constitutional tax powers framing national and regional tax systems with a view not only to solve *functional problems*, but also to ensure *that the tax distributive choices* of each level of government are respected.

On what concerns legislative tax powers, the Union would be expected to acquire full competences over the tax figures which would be collected by the Union itself, while being assigned a variety of legislative powers, aimed at harmonizing bases and rates of taxation, coordinating the exercise of national tax powers, or merely gathering of data with a view to ensure a sound macro-economic policy,

On what concerns collecting powers, the Union would have powers corresponding to the *financial needs* equal to the tasks assigned to it. Moreover, as is typical in federal systems, the Union could act as the collecting agent of nation-states and regions. This solution could be especially pertinent in areas such as the *corporation income tax*. At any rate, the Union would have wide powers concerning the information sharing of national and regional tax administrations.

This implies that the EU should have a budget of its own, mostly funded by taxes directly collected by the Union (i.e. *genuine* own resources, and not national transfers which are called own resources). This should be complemented with a power to borrow in order to finance expenditures with an inter-generational dimension, and to meet cyclical imbalances between revenue and expenditure.

The characterization of the Union as a political community which is part of a cosmopolitan order entails that the taxing powers of the Union should be exerted with a view to ensure *the coherence* of the overall tax system applicable in the Union, that is, the *coherence of the Union, national and regional tax systems*. This requires sheltering, and not hampering, the allocative, redistributive and macro-economic decisions adopted at the national and regional level, especially from the disruptive effects of corporate power.⁶

The main features of the four polity options as outlined above are summarized in Table 8.1 with regard to the different conceptions of European tax power.

⁶ Paradigmatic examples of rights-based discourses on the European tax powers can be found in the federalist and social-democratic literature (Collignon 2004; Strauss-Kahn 2004; see also Menéndez 2004).

TABLE 8.1 DIFFERENT CONCEPTIONS OF EUROPEAN POWERS TO TAX

	PROBLEM-SOLVING	COMMUNITARIAN EUROSCEPTIC	COMMUNITARIAN EURO-NATIONALIST	RIGHTS-BASED
Background distributive justice conception	Liberist	Liberist at the intergovernmental level	Communitarian	Liberal
Constitutional power to tax (EU)	Negative objectives	None	Negative and positive objectives	Negative and positive objectives
Legislative power to tax (EU)	Setting frameworks if needed (preferably tax bases, not rates)	None	Legislating (leaving power to raise additional rates to nation-states)	Co-legislative powers: defining tax bases; fixing rates in some cases
Power to collect (EU)	None; transfers from member states to collect costs	None; transfers from member states to cover administration costs	Most taxes	Concerning taxes which fund the federal level
Systemic relevance	No concern for systemic coherence	No system beyond national tax system	Coherence a task for the federal level	Coherence ensured by joined efforts of all levels of government

IV. The actual tax powers of the European Union

In the following section I will analyse the constitutional, legislative and tax collecting powers of the Union and the economic importance of such powers. This is basically done by means of considering the relative weight of each tax figure over which the Union has powers, both by reference to the Union's GDP and by reference to the total tax collected in the Union. In the absence of a full quantification of the Union's tax powers,¹ it seems to me that the figures highlight the breadth and scope of *Union actual tax powers*, and thus proves wrong the usual assumptions about its negligible tax powers.

A) The constitutional power to tax

The European Union has a wide and extensive *constitutional power to tax*, which affects all European, national and regional taxes. However, the power is basically *negative*, as it does not establish any direct mandate to the legislature concerning the shape of the tax system (as is typical in national constitutions). Moreover, this power is not *exclusive*, but is *co-extensive* with the constitutional powers to tax of member states.

European constitutional norms are an essential part of the *parameter* of constitutionality of European, national and regional tax norms.² European constitutional principles *bind* the legislature on the three levels without exception when drafting tax norms. Indeed, European constitutional principles even extends to the external relations of member states, framing the exercise of the power of member states to enter into agreements with other states (be them member states or third parties) on tax matters (Pistone 2002). There are five groups of prominent principles.

Firstly, the most salient European constitutional norm with tax relevance is the *principle of non-discrimination on the basis of nationality* (Art. 12 TEC). The European Court of Justice (ECJ) has rendered scores of judgments in which national tax norms have been found to be void on account of their formal or material infringement of this principle (see Farmer 2003; Lyal 2003). The Court has declared void not only internal sales taxes which were discriminatory (thus, on the basis of Art. 95 TEC),³ but also personal income tax provisions⁴ and corporate income tax provisions.⁵

¹ This would require measuring the power weight of constitutional, legislative and tax collecting powers, so that all figures could be reduced to one single scale, and added.

² There are also tax implications for EEA members. On this, see e.g. van den Hurk and Theunissen 2001.

³ See e.g. Case 433/85, *Feldain v. Directeur des Services Fiscaux*, [1987] ECR 3536, which was a more sophisticated version of Case 112/84, *Humblot v. Directeur des Services Fiscaux*, [1985] ECR 1367.

⁴ See Farmer 2003; Lyal 2003. Among the cases, see C-175/88, *Biehl*, [1990] ECR I-1779; although the Court finds that national tax measures were contrary to the free movement of workers, in par. 14 it considers as very relevant the fact that the regimes entails a discrimination on the basis of nationality; C-279/92, *Finanzamt Köln*-

Secondly, the four main economic freedoms inscribed in the Treaty, namely, the free movement of goods, persons, services, and capital, along with the principle of free competition.⁶ Indeed, many of the referred judgments of the Court declare national or regional tax norms void on account of a simultaneous violation of the principle of non-discrimination on the basis of nationality and an infringement of one or several of the economic freedoms. The principle of free competition has been increasingly invoked by the Commission as foundation of the claim that some national tax measures qualify as *unlawful* state aid, and therefore should be considered void (European Commission 1996; Schön 1999; Nannetti and Mameli 2002).⁷ The relevance of state aid derives from the extensive practice of having resort to tax expenditures, that is, deductions from the tax liability as a means of fostering certain economic activities or certain products.

Thirdly, the basic principles underlying the Economic and Monetary Union,⁸ and especially the *companion* Growth and Stability Pact,⁹ result, *de facto*, in the framing of the power to tax. The consolidation of Economic and Monetary Union, as established in the Maastricht Treaty, requires a progressive convergence of national macro-economic policies. Specific monitoring and sanctioning mechanisms were annexed to the Amsterdam Treaty concerning excessive budgetary deficits. Moreover, rather detailed broad policy guidelines of economic policy are formulated every year, and the Commission is in charge of reviewing the compliance of national budgets and macro-economic policies with these (see Art. 99 TEC; see also Begg et al. 2003; Hodson 2004). Even if all these provisions do not ground any concrete European constitutional tax power, it is obvious that they result in a further framing of national tax powers, on account of to the *conditions* they impose on macroeconomic policy, including tax policy. This was clearly proved by the 2001 opinion of the Council on the stability programme of Ireland, and more recently and pungently, by the early warnings addressed to Portugal, Germany, Italy and France.¹⁰

Altstadt v. Roland Schumacker, [1995] ECR I-225; C-80/94, *Wielockx v. Inspecteur der Directe Belastingen*, [1995] ECR I-2493, the leading cases on the taxation of non-residents' income; and C-136/00, *Rolf Dieter Danmer*, [2002] ECR I-8147 on deductibility of pension plans contributions.

⁵ See Farmer 2003; Lyal 2003; Jiménez 1999; and, among others, the following cases: Case C-264/96, *Imperial Chemical Industries (ICI)*, [1998] ECR I-4695; Case C118/96, *Safir*, [1998] ECR I-1897; Case C-307/97, *Saint-Gobain*, [1999] ECR I-6161.

⁶ See e.g. Case 270/83, *Commission v. France*, [1986] ECR 273; Case C330/91, *Commerzbank*, [1993] ECR I4017; Case C484/93, *Svensson & Gustavsson*, [1995] ECR I3955; Case C250/95, *Futura Participations*, [1997] ECR I2471; Case C311/97, *Royal Bank of Scotland v. Elliniko Dimosio*, judgement of 29 April 1999.

⁷ See also the 'Commission notice on the application of the State aid rules to measures relating to direct business taxation' of 28 November 1998, OJ C 384 (1998): 3.

⁸ See Articles TEC 99 and 104, and the Protocol on the excessive deficit procedure, annexed to the Treaty of Maastricht.

⁹ See 'Resolution of the European Council on the Stability and Growth Pact Amsterdam', OJ C 236 (1997): 1--2; Council Regulation (EC) 1466/97, OJ L 209 (1997): 1--5; Council Regulation (EC) 1467/97, OJ L 209 (1997): 6--11.

¹⁰ On Ireland, see Council Opinion of 12 February 2001, OJ C 77 (2001) and ECOFIN Council Conclusions of 29 October 2001, SN 4404/01; On Portugal and Germany, see Council Opinion of 12 February 2002,

Fourthly, European tax norms, or national norms which implement European tax legislation (i.e. national VAT legislation), are also bound by the principle of protection of fundamental rights, as spelled out in the solemnly proclaimed Charter of Fundamental Rights. As is the case in many national constitutional systems, fundamental rights establish the *European unconstitutionality* of any tax norms which runs foul of them.

Finally, it must be noted that European constitutional norms establish a basic *distribution of legislative and collecting tax competences*, which bind European, national and regional legislatures. Some of these provisions reflect a basic constitutional choice, as do the prohibition of customs duties affecting trade between member states (Art. 25 TEC). This is akin to a *negative* constitutional tax principle, which extends to quantitative restrictions both to exports and imports, and measures having an equivalent effect (Arts. 27 and 28 TEC). The same can be said of the prohibition to regulate or collect customs on imports from third countries addressed to national and regional legislatures (Art. 26 TEC).

The European relevant constitutional principles regarding tax thus grounds the claim that the Union has *constitutional tax powers* that frame European, national and regional legislation. However, it must be added that most of these powers are *negative*, that is, they set limits to the tax norms that can be written into statutes, without mandating the legislature positive objectives, as is usually the case in national constitutions. This is so because the constitutional power to tax is shared with the member states (and regions) on a rather equal basis. National constitutions and *national constitutional traditions* establish principles that frame all *European* taxes (be them *legally established* by Union, national or regional laws), and that can limit the scope of application of Community principles. Even if these national constitutional traditions are *common*, and as such, they cannot be said to imply some kind of primacy of national over Community law, they prevent raising the claim that the power to frame tax norms belongs within the European Union to the *institutions* of the Union exclusively. Change in the shape and direction of *national constitutional traditions* can actually alter the contents of the framing principles of tax norms in the EU. Further, constitutional principles might come into conflict with each other. Such conflicts require an appropriate *weighing and balancing* of the principles, in order to determine the concrete rule applicable to the concrete case (cp. Alexy 2002). In case of a conflict between a European constitutional principle established at the Community level (e.g. the free movement of capital) and a principle stemming from a national constitutional tradition, the former does not necessarily have preference.

This complex structure is occasionally reflected in the construction of the European legal system by the ECJ. Consider the judgment in *Bachmann*,¹¹ in which the Court argued that a

6108/02 (Presse 28); On Italy, see Council Press Release of 5 July 2004, 10888/04 (Presse 213); On France, see Council Recommendation of 21 January 2003, OJ L 34 (2003): 18--9.

¹¹ Case C-204/90, *Hanns Martin Bachmann v. Belgian State*, [1992] ECR I-249: par. 21--23; Case C-300/90, *Commission v. Belgium*, [1992] ECR I-305: par. 14--16, 20--2.

principle of ‘coherence of national tax systems’, unwritten and unknown until then, required that the contested Belgian national tax norm would be considered as *constitutional*, even if it contradicted *prima facie* the principle of non-discrimination on the basis of nationality and at the very least two fundamental economic freedoms.

The results are mixed. On the one hand, certain principles formulated at the Community level frame the national power to decide the shape of concrete taxes. On the other hand, legislative and collecting tax powers granted to Community institutions must be interpreted in the light of the *common constitutional traditions*. Such common traditions play a major role in deciding potential conflicts between the whole set of principles that frame the European power to tax, be them established through the European or the national constitution-making process.

B) The legislative power to tax

The European Union also has extensive legislative powers to tax. It has exclusive competence on what concerns customs duties and agricultural levies. It has a framing legislative power on what concerns the definition of the tax base of VAT, and considerable powers concerning the determination of VAT rates. It has framing legislative powers concerning the definition of the tax base of excise duties on alcohol, tobacco and mineral oils, taxes collected at rates framed by Union legislation. Furthermore, the Union has limited and fragmentary, but still relevant powers concerning the definition of the corporate income tax and the personal income tax. The Union has full legislative power over *customs duties*, including agricultural, isoglucose and sugar levies. Union powers extend both the definition of the tax base and the setting of tax rates.¹² The Union also has extensive legislative powers on turnover taxes, which has resulted in a long series of directives on VAT.¹³ Such powers are pretty exhaustive on what concerns the definition of the tax base. Not only do all member states collect VAT, but VAT liability is essentially triggered by the very same economic transactions.

Union legislative powers are more of a framing character on what concerns the definition of tax rates. This is so on three accounts. First, member states retain the power to fix the *standard rate* at which VAT is collected within the limits fixed by the Union when setting maximum and minimum VAT rates. Second, member states retain the power to keep up to two reduced rates (see Table 8.2 for the standard and reduced rates in force in the member states).¹⁴ Third, they can exempt a series of goods and services from a list drawn in European legislation.¹⁵ Thus, national autonomy is prevalent, even if it can be exercised

¹² See Council Regulation (EEC) 2913/92, OJ L 302 (1992): 1--50, containing the Community Customs Code.

¹³ The Sixth VAT Directive (Directive 77/388/EEC) of 17 May 1977, OJ L 145 (1977), is the central piece in the European VAT system, as it contains the basic definition of the tax base.

¹⁴ See Article 12.3A of the Sixth Directive. As established by Council Directive 92/77/EEC, OJ L 316 (1992): 1--4, the standard rate has to be at least 15 per cent, while reduced rates should be at least 5 per cent.

¹⁵ See Article 13B of the Sixth Directive.

only within the limits set by Union law (but such limits are, for the time being, rather wide).

The *legislative* powers of the Union over turnover taxes are of major economic importance, given that VAT is one of the three major sources of tax revenue in all national tax systems, representing on average 17.2 per cent of the total tax collected in the EU in 2002. Ireland is the country in which VAT represents a higher percentage of the tax yield (24.8 per cent) while Luxembourg is where VAT is of lesser relative importance (14.9 per cent). Table 8.3 proves that VAT has been one of the major tax figures in the last twenty years. It has consistently represented between one fourth and one fifth of the total tax yield. It can also be noticed that, with the single exception of France (due to the reduction of the standard VAT rate implemented by the left coalition led by Lionel Jospin), VAT seems to be on the increase in terms relative to the total tax yield.

TABLE 8.2 VAT RATES ON MAY 1st, 2003

MEMBER STATE	Super-red.	Reduced	Standard
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Belgium	-	6.0	21.0
Denmark	-		25.0
Germany	-	7.0	16.0
Greece	4.0	8.0	18.0
Spain	4.0	7.0	16.0
France	2.1	5.5	19.6
Ireland	4.3	13.5	21.0
Italy	4.0	10.0	20.0
Luxembourg	3.0	6.0	15.0
Netherlands	-	6.0	19.0
Austria	-	10.0	20.0
Portugal	-	5.0 / 12.0	19.0
Finland	-	8.0 / 17.0	22.0
Sweden	-	6.0 / 12.0	25.0
United Kingdom	-	5.0	17.5

Source: the *Structures of the Taxation Systems in the EU countries, 1995-2002*,
Luxembourg: Office for the Publications of the European Communities, 2004.

**TABLE 8.3 PERCENTAGE OF TOTAL TAX REVENUE STEMMING FROM VAT
(1980, 1998 and 2002)**

MEMBER STATE	1980	Average 1995-2002	2002
Belgium	16.8	15.3	15.4
Denmark	22.3	19.5	19.9
Germany	16.6	16.2	16.2
Greece	13.2	21.3	21.9
Spain	10.2	16.8	16.9
France	21.1	16.8	16.3
Ireland	14.8	22.6	24.8
Italy	15.6	14.2	15.2
Luxembourg	16.4	14.4	14.9
Netherlands	15.8	17.4	19.1
Austria	20.1	18.6	18.7
Portugal	16.2	22.7	22.7
Finland	18.7	17.8	18.2
Sweden	13.4	17.2	18.1
United Kingdom	14.7	18.8	19.3

Source: 1980 data: OECD Revenue Statistics; 2002 data and average 1995-2002 data: the *Structures of the Taxation Systems in the EU countries, 1995-2002*, Luxembourg: Office for the Publications of the European Communities, 2004.

The European Union has extensive legislative powers concerning the definition of the tax base of the main *excise taxes* in all member states, namely *excises on alcoholic beverages, tobacco and mineral oils*.¹⁶ Table 8.4 shows these excises as a percentage of the total tax revenue of the member states. The Union also has framing power concerning the determination of these tax rates. It has not only established the minimum rates,¹⁷ but it has also specified its structure. Union norms are rather exhaustive in this regard.¹⁸ All this implies that the Union has legislative tax powers which extend to taxes yielding between four and ten per cent of the total tax revenue, while the legislative power of the member states is confined to setting the rate of excise.¹⁹

TABLE 8.4 PERCENTAGE OF TOTAL TAX REVENUE STEMMING FROM EXCISES ON ALCOHOL, MINERAL OILS AND TOBACCO (1998)

MEMBER STATE	Tobacco	Alcohol	Mineral Oils	Total
Belgium	1.12	0.55	3.28	4.95
Denmark	1.28	0.74	1.54	3.56
Germany	1.54	0.48	4.76	6.78
Greece	4.27	0.80	8.94	14.01
Spain	n.d.	n.d.	n.d.	n.d.
France	1.18	0.48	4.07	5.73
Ireland	3.20	3.15	5.34	11.69
Italy	1.09	0.15	5.08	6.32
Luxembourg	4.17	0.39	6.39	10.95
Netherlands	0.96	0.38	3.47	4.81
Austria	1.30	0.79	3.07	5.16
Portugal	2.87	0.54	7.51	10.92
Finland	1.06	2.26	4.82	8.14
Sweden	0.76	1.01	2.45	4.22
United Kingdom	2.40	1.87	6.65	10.92

¹⁶ See Council Directives 92/83/EEC of 19 October 1992; 95/59/EC of 27 November 1995; and 92/81/EEC of 19 October 1992.

¹⁷ See Council Directives 92/79/EEC, 92/82/EEC and 92/84/EEC of 19 October 1992; and 1999/81/EC of 29 July 1999, OJ L 211 (1999): 47.

¹⁸ Consider, for example, excise duties levied on cigarettes, which account for at least 57 per cent of the retail selling price (including all taxes, cigarettes belonging to the most popular price category).

¹⁹ See also Council Directive 92/12/EEC, OJ L 76 (1992): 1, as last amended by Directive 2000/44/EC, OJ L 161 (2000): 82.

The Union has fragmentary legislative powers limiting the tax liability which member states can establish on account of *corporate income taxes*. Such powers have been exercised through three directives.²⁰ However, it must be acknowledged that such directives are specific concretizations of the Union constitutional tax principle of non-discrimination on the basis of nationality, specifically on what concerns cross-border economic activities undertaken by companies, and of the freedom of establishment and the free movement of capital. As such, they reflect more the constitutional tax powers than the legislative tax powers of the Union. In addition, a Code of Conduct on business taxation was approved in 1997,²¹ and a report on its basis published in 2000.²² This Code had a limited but not irrelevant impact on the definition of national corporate income tax bases. However, the Code was not presented as a *binding piece of legislation*, but as a piece of soft law, from which no further tax powers accrued to the Union.

Another area where the Union has fragmentary legislative powers concerns the definition of *personal income taxation*, more specifically on what concerns *income stemming from savings in the form of interest payments*.²³ This power (see Art. 6 of the Directive) comes hand in hand with a power to fix the rate at which a withholding tax should be collected on savings income obtained in a member state by a national of another member state. The EU rate (35 per cent at the end of the transitional period) is applicable only if the member state where the interest payments take place does not *automatically report* to the member state of residence of the person receiving the payment that such income has accrued to her (Arts. 8 and 9).

This implies the affirmation of a positive legislative power on what concerns the definition of the *personal income tax base*, and the accrual of a conditional full legislative power in case that the member state does not opt for the automatic exchange of information with other member state. The *economic* importance of this power cannot be properly established by reference to the present relative weight of capital income taxation, if only because the levels of tax avoidance are rampant (in part as a result of the affirmation of free movement of capital as an autonomous economic freedom since 1988). However, some estimate that

²⁰ The merger directive (Council Directive 90/434/EEC, OJ L 225 [1990]: 1--5) articulates a basic negative legislative decision. The parent-subsidiary directive (Council Directive 90/435/EEC, OJ L 225 [1990]: 6--9) determines the tax treatment that national tax legislations should give to benefits transferred from a subsidiary to a parent company established in another member state. The directive on a common system of taxation applicable to interest and royalty payments made between associated companies of different member states (Council Directive 2003/49/EC, OJ L 157 [2003]: 49--54) aims to avoid double taxation of interest and royalty payments in cross-border payments between associated companies, which implies a legislative measure aimed at allocating the power to tax certain corporate income tax bases among member states.

²¹ Annex to the Conclusions of the ECOFIN Council Meeting on 1 December 1997, concerning taxation policy, OJ C 2 (1998): 2--5.

²² See the report of the ensuing group (the Primarolo Group) to the ECOFIN Council, Press Release 4901/99 of 29 February 2000; see also Radaelli 2003.

²³ Council Directive 2003/48/EC, OJ L 157 (2003): 38--48, for its application, see OJ L 257 (2004): 7. See further Larking 2001; Dassel 2004; and the well-argued criticism in Pires 2002. A political science analysis in Holzinger 2003.

the measure, if fully functional, will report between two and three per cent of the present total tax revenue yield (Drèze and Malinvaud 1994).

With the only exception of customs duties, agricultural, sugar and isoglucose duties, all these legislative powers are subject to the law-making procedure established in Art. 94 TEC, in conjunction with Art. 95.1 TEC. This subjects the approval of the proposals made by the Commission to unanimous agreement in the Council. Such a procedure clearly favours the maintenance of the status quo, and casts a shadow upon the strength of Union legislative tax powers. However, this is not exactly the same as preserving *national tax sovereignty*. Once legislative powers have been exercised, member states are bound by Union legislation until it is amended. This might have entailed a *de facto* transfer of power from public institutions to markets, which can indulge into tax-shopping practices. But I would like to insist that it would be wrong to derive from this state of affairs that *nation-states* have retained most of their national tax sovereignty. Finally, it must be added that in the case of customs and agricultural duties, a qualified majority in the Council is sufficient (Art. 36 TEC).

C) Tax collecting power

The third dimension of the power to tax corresponds to the power to actually collect taxes. The powers of the Union are limited, but still far from negligible. The Union has tax collecting powers over customs and agricultural duties, in addition to having established a framework within which national tax administrations must act in defence of the revenue interest of the Union and of other national tax administrations.

a) The tax bases of the Union

Leaving aside the power to collect personal income taxes over the wages paid to its own employees, characteristically granted to all international organizations, the Union is entitled to collect all customs duties on goods and services imported in the Union from third countries (with basis on Art. 26 TEC), as well as agricultural, sugar and isoglucose levies. It also has a legal title to a percentage of the VAT collected in all member states.²⁴ These powers are usually neglected or unknown because the taxes are *effectively collected* by public servants which taxpayers perceive as *exclusively national public servants*.

In the case of VAT, the fact that a part of the rate goes to the Union is obscured by the fact that this is not advertised to citizens in any European country, and even more by the fact that the concrete amount is not directly determined in each and every transaction, but by reference to a complex, aggregate formula. This is due to the very simple fact that the definition of the tax base and of the products and services subject to VAT is not fully

²⁴ See Council Decision 2000/597EC, EURATOM on the system of the European Communities' own resources, OJ L 253 (2000): 42--46

harmonized (in that member states retain some marginal powers). VAT is thus in practice *transferred* from the budget of each member state to Union coffers, in exactly the same manner as the national contributions proportional to the national income are handed over. Indeed, this is usually marked as a *national transfer* in *national budgets*. This can only breed confusion over the *Europeanness* of the EU VAT rate. To make things even worse, the decision over the specific EU VAT rate is subject to a decision-making procedure equivalent to a Treaty amendment (the own resources decision) (see Art. 269 TEC). Nothing could render the existence of an actual power to collect VAT more obscure to European citizens. Similar observations can be made on what concerns customs and agricultural levies, collected by national agents *acting on behalf of the Union*, but whose institutional identity in the eyes of the public remains national.

Moreover, the Union is constitutionally precluded from issuing debt, and must have a balanced budget (Art. TEC 268).

These taxes give the Union a modest power to collect taxes. Their aggregate yield represents less than one per cent of the European GDP (0.5 per cent of the GDP of the EU--15 in 2002, an average 0.7 per cent in the period 1995--2002), which amounts to less than two per cent of the total amount of taxes paid in the Union (a meagre 1.23 per cent in 2002, and an average 1.72 per cent in the period 1995--2002).²⁵

However, to come to the conclusion that such powers are basically negligible, as many do, is a trifle precipitated.²⁶ On what concerns the power to collect customs duties, the *importance* of the decision taken *in principle* in the Rome Treaty of 1957, and actually implemented in 1970, can only be fully appreciated if one considers the *actual* relative weight of customs duties in the 1950s and 1970s, and not their present weight. Otherwise, one incurs in an anachronistic reading of the decisions. As late as 1965, customs duties yielded to member states well over two per cent of their tax revenues; with the Netherlands (over six per cent) and Luxemburg (under 0.5 per cent) being the two deviant cases (see Table 8.5). It was not fully unpredictable that the yield of customs duties would decline as international trade in goods and services became increasingly deregulated, but this supposed joining together of a small but far from insignificant amount of the tax revenues of member states.

TABLE 8.5 CUSTOMS DUTIES AS PERCENTAGE OF TOTAL TAX REVENUE

²⁵ The data is taken from *Structures of the Taxation Systems in the EU countries*.

²⁶ For example Moravcsik (2003: 608) does: 'At a first approximation, the EU does not tax, spend, implement or coerce and, in many areas, it does not hold a legal monopoly of public authority (...) The ability to tax and spend is what most strikingly distinguishes the modern European state from its predecessors, yet the EU's ability to tax is capped at about 2-3% of national and local government spending (1.3% of GDP) and is unlikely to change soon.'

COUNTRY	1965	1998
BELGIUM	4.24	1.17
FRANCE	1.82	0.23
GERMANY	2.23	0.46
ITALY	2.57	0.26
LUXEMBOURG	0.45	0.35
NETHERLANDS	6.40	1.30

Source: OECD 1999 Revenue Statistics.

b) Powers instrumental to tax collection

A 1976 Directive marked a clear break with two ideas central to national tax administrations, namely, that they had to monitor compliance with national tax laws and defend the national revenue interest -- *national* in both cases being exhaustive of the laws to be applied and of the revenue interest to be protected. Indeed, the directive required national tax administrations to treat requests from other member states almost as they were stemming from the own national tax administration; thus *recognizing and enforcing the tax claims made by the tax administrations of other member states*. At first, the scope of application of the norm was limited to the taxes over which the Communities had been assigned tax collecting powers: customs duties and agricultural duties.²⁷ However, the field of direct taxation was covered by a Directive approved the following year, which imposed a duty to share information among national tax administrations.²⁸ As time has passed, the scope of both directives has tended to increase, thus reinforcing the process of Europeanization of national tax administrations.²⁹

The net upshot of this analysis is that the taxing powers of the EU include: wide constitutional tax powers affecting all tax norms, but which are mainly negative and not-exclusive, as national constitutional tax principles keep on playing a major role; extensive legislative powers affecting the definition of the tax base of almost half of the total amount of taxes collected in the Union, although such powers are weaker on what concerns personal and corporate income taxation, and the economic importance of which is somehow relativized by the requirement of Council unanimity for their exercise; and, finally, rather limited tax collecting powers, although coupled with a thick normative

²⁷ Council Directive 76/308/EEC, OJ L 73 (1976): 18--23.

²⁸ Council Directive 77/799/EEC, OJ L 336 (1977): 15--20.

²⁹ Council Directive 2001/44/EC, OJ L 175 (2001): 17--20; the Commission Directive 2002/94/EC, OJ L 337 (2002): 41--54, lays down detailed rules for implementing certain provisions of Council Directive 76/308/EEC on mutual assistance for the recovery of claims relating to certain levies, duties, taxes and other measures.

framework which reconfigures the very institutional identity of national tax administrations.

V. Which Model Fits Better?

I started out this chapter by sketching three different conceptions of the European Union, and postulating the corresponding characteristics of the Union's tax powers. I then proceeded with an analysis of the actual constitutional, legislative and collecting tax powers of the Union. I am thus now in a position to discuss which of the three conceptions corresponds more closely to the actual powers of the Union.

A) The communitarian model

A first conclusion is rather easy to reach. The communitarian conception of the Union, either in its Euro-sceptic or Euro-national model, is clearly not one which corresponds to the present taxing powers of the Union. The Euro-sceptic variant fail to explain the extensive constitutional, legislative and collecting taxing powers of the Union. Further, the present taxing powers of the Union fall short of what is implied by the Euro-national communitarian conception. One would expect more *positive* constitutional powers, more extensive *legislative* powers, and clearly far reaching tax collecting powers. It must be concluded that while the Euro-sceptic conception has been factually transcended, the Euro-nationalist conception seems a rather far-away normative vision, not least because the respect of the identity of member states as political communities is part and parcel of positive constitutional Union law.

This leaves us with two paradigms competing as the most plausible framework within which to reconstruct the present taxing powers of the Union, the *problem-solving* and the *rights-based* conceptions. While a *static* reconstruction seems to indicate that the former conception fits better the present shape of the taxing powers of the Union, a *dynamic* reconstruction of the taxing powers of the Union increases the salience of the rights-based conception. This leads me to the conclusion that the taxing powers of the Union are in transition from a *problem-solving* paradigm to a *rights-based* one.

B) The problem-solving model

The EU's most outstanding powers are no other than negative constitutional tax powers and limited legislative powers specifically aimed at establishing the tax conditions under which the common, and later, single market could function. The completion of the common market, and also the resolution of the problems deriving from the success of market-making, explain why powers have been transferred to the Union. Tax collecting powers in the hands of the Union are limited, and they are closely related to the financing of a limited range of policies which are in themselves indicative of the commitment to a common institutional framework.

Advocates of regulatory governance can argue in support of their claims that official discourses on the taxing powers of the Union are clearly reflective of the conception of the Union as a tax problem-solver. Even a superficial reading of the Commission's policy papers and proposals of the last decade points in this direction. Indeed, the Commission's discourse has focused on justifying its proposals by reference to possible welfare gains. In this regard, the emphasis on so-called tax coordination comes hand in hand with the abandonment of legislative proposals of a more systematic character. The very idea of 'tax package', comprising the late 1990s tax initiatives, does not point to the construction of a *European tax system*, even in a piece-meal fashion, but merely to a package deal. Finally, one could argue that not much has been done to reduce the levels of tax fraud rendered possible by the very process of European integration. Indeed, not even the call to curb *harmful* tax competition is yet translated into the adoption of concrete measures, something which might be said to indicate that the very idea of national tax sovereignty trumps the characterization of the Union as a true political community. Member states can see themselves as players in a competitive game where *self-interest* and *self-gains* prevail over a *communal* sense of fairness. One must however adjust for the very *dynamics* through which the present configuration of taxing powers of the Union has come about.

C) The rights-based model

First, one must take into account that the assignment of additional legislative taxing capacities to the Union has not always been justified with reference to narrow and specific problems, and the exercise of the existing, transferred powers is usually motivated by more comprehensive goals. It is clear that the transfer of legislative competences over the definition of the savings income tax base, or plans to assign legislative competences over the definition of the corporate tax, have been justified and discussed by reference not only to the consequences that the lack of harmonization has over competition in the single market, but mainly by reference to the erosion of the tax powers of member states and the consequences that this has in terms of vertical and horizontal tax equality, and especially on the financial basis of welfare states. The evolution of Union powers on VAT offers good examples of this. The approval of the Sixth VAT Directive in the early 1970s resulted in the harmonization of the definition of the tax base of turnover taxation. This was actually required not so much by the need to perfect the common market (as this was essentially achieved with the First and Second VAT Directives of the late sixties), but by the decision to assign to the Union a rate of the Value Added Tax collected in the whole Union, as part of its own resources. Moreover, the Union has recently started to make use of VAT as a macro-economic lever. More specifically, reduced VAT rates were allowed on two types of services which were labour-intensive; the overall goal was to make use of the legislative tax power of the Union in order to reduce unemployment.³⁰

³⁰ Council Directive 1999/85/EC, OJ L 277 (1999): 34--6; prolonged by Council Directive 2002/92/EC, OJ L 331 (2002): 27. Detailed information on its application can be found in the Commission press release (IP/99/1002) of 20 December 1999.

Second, it might be the case that public discourses on European tax powers and norms are constructed upon a problem-solving conception of the Union. However, this might be somehow misleading. It is clear that, as the Treaties stand, the accrual of new tax powers to the Union must be justified by reference to the very idea of single-market making. However, the definition of the problems and challenges which the Union confronts requires solutions which clearly transcend the problem-solving conception of the Union. In brief, we might be close to the point in which spillovers become *political*. A good illustration of this point is provided by present discourses on European corporate taxation. True, the repeated failures of attempts at harmonizing even limited parts of the corporate income tax,³¹ and the limited scope of legislative tax powers actually in the hand of the Union could be explained by the rationales behind the problem-solving conception. Moreover, a first reading of the most recent Communications and studies of the Commission on the matter seems to justify the accrual of further competences to the Union by reference to specific problems of an economic or technical character.³² In the official (and dominant) discourse the corporate income tax is a question that the Union has to address because the present state of affairs leads to a distortion of the levelled playing field which the single market should provide to economic actors. As things stand, efficiency losses are incurred, and the international competitiveness of European companies is hampered. A technical, welfare-based argument is clearly made when reference is made to the fact that cross-national companies incur losses as they have to comply with as many accounting systems as the member states they operate in, when corporations sometimes are double-taxed, or when cross-border restructuring is penalized by taxes which will not be due on purely internal operations. Still, what is hard to explain from the problem-solving perspective is that the discourse has increasingly focused on the need of transcending targeted solutions (as the parent-subsidiary or merger directives). A structural reform of corporate income taxation, nothing less, is required in order to solve present problems. This implies a quantitative leap in the discourse. True, the discourse keeps on affirming that the very reason why this reform should be undertaken is the very idea of completing the single market. But the concrete measures have open political implications, as is simultaneously acknowledged. More specifically, the Commission argues that there is a need for a European definition of the corporate income tax base applicable at the very least to the corporations making use of the European Company Statute, and eventually to all big companies.³³ Further, a mutual

³¹ Proposals of corporate tax harmonization were already formulated in the early 1960s, see Regul and Renner 1966: 116--7. A comprehensive proposal was made in 1975 (European Commission 1975). While some support seemed to exist for the harmonization of tax rates (with the Commission proposing rates between 45 and 55 per cent), the same could not be said about the harmonization of tax bases, which was regarded as exclusive competence of the member states. The failure of the proposal entailed that, until very recently, proposals were very limited in breadth and scope.

³² See European Commission 2001b; the companion and more thorough working paper of the Commission staff (SEC (2001) 1681); and the recent follow-up by the European Commission (2003).

³³ For a study on tax implications, see the 'Survey on the Taxation of the Societas Europaea' of 2003, by the International Bureau of Fiscal Documentation.

recognition of national tax base definitions should be the solution applicable to small and medium-sized corporations, and at the very least, experimented for some years.³⁴

This explains why the harmonization of corporate tax bases is back on the agenda of the Council.³⁵ The mutual recognition of national tax systems or some form or another of European corporate tax might be justified with a view to *render perfect* the common market, but they are much more than ordinary spillovers. Indeed, as neo-functionalists could agree, they are spillovers which reveal the open political character of the whole process of market-making, since its very beginning. Similarly, problem-solving conceptions also have a hard time explaining new elements in the corporate tax discourse. For example, there is a growing number of references to the mismatch between the existence of a ‘single market’ and twenty-five corporate tax systems; if profits are made on a European wide scale, why should they be taxed on a national scale? Such questions clearly raise the issue of which community is of economic risk in a single market. Furthermore, these new lines of argumentation are openly supported by several national governments, which simultaneously invoke *market-making* arguments (the need of completing the common market), and *political reasons*, which reveal the connections between corporate taxation and distributive justice (tax dumping leads to social dumping).³⁶ Hence the emergence of social movements and political platforms which request a degree of corporate tax harmonization *mainly* on political reasons.³⁷ It does not take much ingenuity to realize that the Eastern enlargement probably will exacerbate tensions, and further render explicit the political character of the discourse on the matter. The fact that some of the new member states (significantly, Cyprus, Latvia and Lithuania) have an effective corporate tax rate

³⁴ See the Commission’s ‘Outline of a possible experimental application of Home State Taxation to small and medium-sized enterprises’, DG XXI, TAXAUD C.1/doc (04) 1410, 24 June 2004.

³⁵ See ‘Commission Non-paper to informal Ecofin Council of 10 and 11 September 2004: A Common Consolidated EU Corporate Tax Base’, of 7 July 2004; ‘Commission Non-paper to informal Ecofin Council of 10 and 11 September 2004: Home State Taxation for Small and Medium-Sized Enterprises’, of 7 July 2004; ‘Results of Informal Meeting of Economics and Finance Ministers, The Hague, 10–11th September 2004 -- Banking and Company Taxation’, MEMO/04/214 of 13 September 2004.

³⁶ The discussion is old, but was revived by enlargement. On the eve of enlargement, Gerhard Schroeder openly linked corporate tax harmonization and solidarity between Member States of the European Union. See ‘A double edge sword’, *The Economist*, 30 April 2004. This claim was also made by the French Chancellor of the Exchequer, see ‘The Nicholas v Jacques show’, *The Economist*, 11 September 2004. See also ‘Tax Wars in the EU’, *The Economist*, 24 July 2004. Political pressures based on the connection between tax dumping and social policy were acknowledged by the Director General for Taxation, Robert Verrue, before the Economic and Monetary Committee of the European Parliament, see ‘Commission hopes to launch co-operation on company tax’, *Agence Europe*, 2 September 2004. See also ‘Le dumping fiscal empoisonne les relations franco-polonaises’, *Le Monde*, 11 September 2004; ‘La Pologne revendique l’utilisation de l’arme fiscale pour créer des emplois’, *Le Monde*, 14 September 2004; ‘Bruxelles songe à harmoniser l’assiette de l’impôt sur les sociétés’, *Le Monde*, 14 September 2004: ‘Officiellement, les délocalisations n’étaient pas au menu de la réunion des ministres des finances européens, qui s’est tenue à La Haye vendredi 10 et samedi 11 septembre. Mais le sujet occupait tous les esprits’.

³⁷ Which ends up affecting the political platforms of traditional political parties. See e.g. the European Socialists manifesto on globalisation, ‘Europe 2004: Changing the Future’, of 5 February 2004.

which represents one third to half of the effective tax rate of present member states ensures that the issue will not simply go away.³⁸

Third, the fragmented and non-systematic character of the legislative and collecting tax powers of the Union reflects the disjointed character of public expenditure of the Union. However, it is no less true that what apparently are disparate programs can be reconstructed from the standpoint of basic legal principles in order to justify a further expansion of taxing and expenditure in the hands of the Union. In that regard, the introduction of the principle of social and economic cohesion in the Single European Act (Articles TEC 158 to 162) has served to provide a common focus to the expenditure programs approved since then, and might play an essential role in further moving the European tax powers in the direction of a rights-based political order.

Fourth and finally, European tax powers are exercised within the constitutional and legal framework provided by the European Union legal order. This is based on the basic principle of loyalty among member states, which points towards a sense of solidarity and commonality which goes far beyond the idea of a mutual advantage contract. It implies a commitment to institutionalization which goes beyond the mere projection of credibility. This contributes to a formal or thin *we-feeling*, upon which European tax norms can further build. Indeed, the *Europeanization* of national tax administrations, the obligation to defend the revenue interest of the Union and of the other national tax administrations creates *some of the conditions* under which a we-feeling can be forged in a civic, solidaristic fashion.

Conclusions

On the background of a theoretical framework for analyzing the division of taxing powers between the Union and its member states, I examined the actual constitutional, legislative and collecting tax powers in the hands of the Union. What do such powers tell us about the nature of the Union as a political community? I analyzed which of the three basic polity models of the EU (as a problem-solving, communitarian or rights-based polity) fits better the set of tax competencies in the hands of the Union. While it is concluded that the Union's tax powers are far wider than commonly asserted -- partly due to the influence exerted on national and regional taxing powers by the Union's constitutional and legislative tax powers -- it is found that the Union still presents most of the features characteristic of a regulatory entity.

Having said that, a dynamic reconstruction of these same powers indicates that the Union is moving towards a rights-based polity, also on what concerns its taxing powers. There are clear indications that the *problem-solving* paradigm is not enough, and increasingly will not be so, to explain and ground the powers to tax in the hands of the Union. This is because:

³⁸ On effective corporate tax rates in the new member states, see the 2004 report of Ernst and Young, 'Company Taxation in the New EU Member States: Survey of the Tax Regimes and Effective Tax Burdens for Multinational Investors'.

- the assignment of tax powers to the Union, and its actual exercise, is increasingly justified by reference to conceptions of tax and economic justice;
- even in those cases in which the assignment of new taxing powers is justified by reference to functional purposes, the solutions proposed imply a transcendence of a pure problem-solving paradigm, as they entail a *political spillover*;
- the affirmation of the principle of social and economic cohesion as part and parcel of European constitutional law might trigger a recharacterization of the purpose of EU taxing powers;
- the regulation of EU taxing powers by an increasingly constitutionalized Union legal order points to a sense of solidarity and commitment which transcends the mutual-gain basis of a problem-solving conception.

Our political representatives and most fellow citizens might still think of the Union as a tax problem-solving entity; it might even be true that they feel at ease discussing tax questions within the confines of such a paradigm. But it is increasingly difficult to pretend that the issues being raised can be dealt in mainly non-political terms, in brief, in terms different from those in which tax questions are posed within Member States. Basic principles of Union constitutional law, not to talk of the factual dynamics of economic integration, rule out many tax decisions which were perfectly conceivable only two or three decades ago. The introduction of reduced VAT rates to foster the creation of employment, the definition of savings income tax bases, or the fixation of corporate income tax bases are the kind of questions around which elections are fought and decided; they have been set or are in the process of being set at the European level, through a European decision-making process. Moreover, the taxing powers of the Union are but a part, even if an essential one, of the set of public powers in the hands of the Union. The constitutional turn of the Union as a whole, seems to point towards the transformation of the Union into a political community, which cannot be stable and sustainable without a we-feeling created and regenerated through the exercise of taxing powers.

Taxation without representation is tyrannical, but representation without taxation cannot but end up putting into risk the fabric of the Social Rechtsstaat which the Union claims to be.

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