



Reconstituting Democratic Taxation in Europe

The conceptual framework

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Abstract

This paper explores how and to what extent it is possible to contribute to the Democratisation of the European political order by means of modifying the ways in which taxes are deliberated upon, decided and collected in the old continent. In the first part, the author elucidates the particular relationship which prevails between the institutional setup and the decision-making processes of the European Union, the structure of the European tax order and democratic legitimacy, and concludes that No European Democracy without European Taxation. In the second part, the three general RECON models are specified by reference to four dimensions of any tax order, and thus the ground is laid to the study of both the emergence of a supranational tax order and the Europeanisation of national tax systems, which will be conducted in coming papers.

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Introduction

This paper is the first in a three-fold series which aims at exploring how and to what extent it is possible to contribute to the democratisation of the European political order by means of modifying the ways in which taxes are deliberated upon, decided and collected in the old continent. This paper has two main aims. In the first part, I consider three reasons why there is a close connection between taxation and democracy, and consequently, why taxes should be of concern for all those interested in democracy in Europe. Firstly, raising and spending taxes¹ have major political, economic and legal implications. There is thus a close and reciprocal relation between the democratic legitimacy of taxation and the democratic legitimacy of the political order as a whole. Secondly, the transformation of national tax systems has been at the core of the process of economic and political integration which has led to the creation and consolidation of the European Communities. The transfer of taxing powers to the European Union, and the parallel convergence of national tax systems around supranational standards, have been two major processes through which European integration has been realised. The third reason is that integration has altered the economic consequences of the national tax systems, in that the degree of realisation of the constitutional principles of tax justice (and of constitutional principles in general) has been slimmed down. In the second part of the paper, I apply the three general models of what the European Union is and/or should be, which are fleshed out in the RECON research project, to the European tax problematique. In concrete, I consider the implications of each of the three RECON models on four key taxing questions: (1) what is the purpose of the common European market; (2) what is the purpose of tax system(s); (3) which are the proper procedures of taxing decision-making; and (4) which substantive principles should be realised in order to render tax system(s) stable over time.

This paper outlines the analytical framework on which the other two papers in the series will proceed to reconstruct (1) the present assignment of taxing powers in the European Union and (2) the process of Europeanisation of

¹ Taxes are here defined in general terms as transfers of resources from individuals to public institutions for the purpose of providing material resources with which to finance the tasks that have been assigned to public institutions. I have discussed this definition in *Justifying Taxes*, Dordrecht: Kluwer, 2001

national tax systems over time. The series as a whole will allow drawing some conclusions on the validity of each of the three RECON models in the tax field.

Taxation, democracy and European integration

The design of a tax system presupposes that fundamental political, economic and legal arrangements are in place, and thus that questions relevant to any democratic theory of the European political order have been answered. As was claimed in the introduction, there is a close and reciprocal relation between the democratic legitimacy of taxation and the democratic legitimacy of the political order as a whole (“no democracy without taxation”). Consequently, the procedures through which decisions on the design of the tax system are adopted are key templates of democratic decision-making in general. Moreover, the normative substance which underpins democratic legitimacy – essentially, the civil liberties and fundamental rights presupposed by even the most abstract idea of democratic government – requires that the design of the tax system ensures the legitimacy of the socio-economic order as a whole. One could thus say that taxation is the collateral of the democratic legitimacy of the socio-economic order. Finally, the stability of a democratic political order relies to a great extent on a certain level of provision of public goods and services, as well as redistribution of economic resources, which rely on the tax system within the socio-economic constellation that is characteristic of ‘capitalist’ economies (taxation as the price of civilisation). Let us consider these claims in more detail.

No democracy without taxation: The procedures through which the norms of taxation are set up and implemented play a paramount role in shaping collective decision-making in general. The historical development of democracy² was closely associated not only to the development of modern

² Democracy is here defined as what is often referred to as ‘modern democracy’, i.e. the concretization of the ideal of self-rule from the French Revolution onwards. The ideal of democracy is clearly much older, but the characterization of democratic politics as a process through which the multitude of individual preferences is transformed into the general will in a legitimate way is clearly modern. On the question, see Anthony Arblaster, *Democracy*, Milton Keynes: Open University Press, 1987 and Luciano Canfora, *Democrazia: storia di un’ideologia*, Bari and Roma: Laterza, 2004. Indeed, debates such as those engaging British politics in the 17th century can retrospectively be looked at as a contest to define who the

economic systems of production, but also to controversies over the concrete design of such systems, and in particular, over the allocation of the power to tax and the design of the emerging tax system. Indeed, the three 'great' liberal revolutions, i.e. the 1688 Glorious Revolution, the 1774 American Revolution and the 1789 French Revolution,³ all had their immediate origin in disputes over whether the royal prerogative enabled kings to collect taxes without the consent of Parliament, or whether, on the contrary, the principle of 'no taxation without representation' should be at the core of any legitimate political order.⁴ The establishment of representative institutions in a handful of countries could be partially attributed to the dexterity and political savvy of parliamentarians who used their power of the purse strategically so as to increase overall political influence.⁵ It is also rather well known that contemporary democratic constitutional frameworks tend to contain a sophisticated array of law-making procedures concerning taxes. This typically includes specific processes of general will-formation on budgetary and tax laws; and usually also either specific procedures applicable to the implementation of tax norms through regulations elaborated by national

'people' are (the King as their embodiment by divine fiat; the Parliament as representative of citizens; or the Army, as being their closer representative). But this was not the language in which the debate took place, and it was indeed the very authors which inspired movements such as the Levellers who coined such a language. See Edmund S. Morgan, *Inventing the People: The rise of popular sovereignty in England and America*, New York: Norton, 1989.

³ The 1917 Russian Revolution, even if a major turning point in world history, was a socialist, not a liberal revolution. And although the tax burden of the farmers helped gathering the storm in the preceding years, the casual link is more tenuous than in the liberal trio. While the 1905 revolution following the Russian-Japanese war was stirred by higher taxes to pay for the conflict, the setting of the October 1917 revolution was the First World War, and the traumatic experiences that followed. The revolution was triggered by the intrinsic instability of the regime, and directly fuelled by the daring life conditions of Russians during the war. See Sheila Fitzpatrick, *The Russian Revolution*, Oxford: Oxford University Press, 1982.

⁴ See among the historical literature, John Brewer, *The Sinews of Power: War, Money and the English State*, Cambridge: Harvard University Press, 1990; John Phillip Reid, *Constitutional History of the American Revolution: The Authority to Tax*, Madison: University of Wisconsin Press, 1987; Michael Kwass, 'A Kingdom of Taxpayers: State Formation, Privilege, and Political Culture in Eighteenth-Century France', 70 (1998) *The Journal of Modern History*, pp. 295-339; id., *Privilege and the Politics of Taxation in Eighteenth-Century France: Liberté, Egalité, Fiscalité*, Cambridge: Cambridge University Press, 2000.

⁵ Cf. Michael Ross, 'Does Taxation lead to Representation?', 34 (2004) *British Journal of Political Science*, pp. 229-49.

administrations or complex governance mechanisms which allow for the participation of taxpayers themselves.⁶ Taxing powers thus provide a concrete template on the basis of which to shape the principle of legality.⁷

Taxes as the guarantee of the legitimacy of the socio-economic order: The legitimacy of a political order critically depends on the distributional capacities of the tax system. European (and in general, Western)⁸ societies are characterised by a form of division of labour which comes hand in hand with the allocation of private property rights, the legal acknowledgment and protection of corporations as legal persons,⁹ a hierarchical organisation of workplaces (in which entrepreneurs and their agents command workers) and the exchange of goods and services through markets (in brief, capitalism).¹⁰ There is certainly a wide range of possible conceptions of private property (in particular concerning the legal powers granted to capital owners), hierarchical labour

⁶ This is usually multinational corporations. See Sol Picciotto, *International Business Taxation*, London: Weinfield and Nicholson, 1992.

⁷ See my *Justifying Taxes: Some Elements for a General Theory of Democratic Tax Law*, Dordrecht: Kluwer, 2001. On the general influence of tax law on public law, see the classic contributions of Albert Hensel and Ottmar Bühler, 'La Influencia del Derecho Tributario sobre la construcción de los conceptos del derecho público', 22 (1973) *Hacienda Pública Española*, pp. 173-206.

⁸ The term 'Western' is clearly problematic but is used here for simplification only, being fully aware of the political and normative wrongs which derive from the distinction between West and East. On that point, see Edward Said, *Orientalism*, London: Routledge, Kegan and Paul, 1978.

⁹ It is conceivable to organise a socio-economic structure around private property and market exchanges where the right to establish corporations is very limited. But although analytically and normatively speaking the questions are distinct, in practice the socio-economic structure of all countries which are members of the OECD is one in which private property, private enterprise and market exchange are key institutional pieces. On the history of the corporate form, see John Micklewhait and Adrian Woolridge, *The Company*, New York: Modern Library, 2003. Joel Bakan, *The Corporation*, New York: Free Press, 2004 (and the companion documentary film) is a scathing criticism of the pathologies of the capitalist corporation. Scott R. Bowman, *The Modern Corporation and American Political Thought*, University Park: Pennsylvania University Press, 1996 is the best account of the history and present of the corporation from the standpoint of legal and political theory.

¹⁰ On the history and normative problematique of private property, see Alan Ryan, *The Right to Private Property*, Oxford: Basil Blackwell, 1984. On why we should use the term 'capitalism' or 'corporate economy', the arguments made by the late John Kenneth Galbraith are rebuttal-proof. See *The Economics of Innocent Fraud*, Harmondsworth: Penguin, 2005.

relations, corporations and markets (entailing different characterisations of the substance and regulatory framework of each of them), which result in different conceptions of capitalism.¹¹ But no configuration of the socio-economic order is capable of providing its own legitimacy. On the contrary, its legitimacy is crucially dependent on the simultaneous provision of a minimum level of goods and services according to the needs of each recipient, and the redistribution of economic resources so that all citizens not only can exert the capabilities of a democratic citizen, but also see the socio-economic order as mutually profitable. Indeed, the tax system is the institution which operationalises the ensuing obligations and thus establishes the foundation for the legitimacy of the socio-economic order as a whole. In other words, the tax system *as a system* is the complex formula that allows citizens to calculate the value of what they owe to the community,¹² and consequently, to all their co-citizens, and in particular, those less advantaged by the prevailing socio-economic system. The existence of public institutions, which provide public goods and services and redistribute economic resources so as to satisfy demands both of commutative and distributive justice, allow citizens to share the burden. By this, the tax system not only reduces cognitive uncertainties and provides additional motivational grounds, but is crucial to the legitimacy of the political order as a whole. In brief, taxes should be viewed as the collateral payment which renders the socio-economic order as a whole legitimate.¹³ This is why no (modern) polity can claim to be legitimate if there is not a legitimate *and* efficient procedure for the designing of norms governing the tax system, which is a requisite for collecting taxes.¹⁴

Taxes as the price of civilisation: The sustainability and stability of a political order over time depends on the legitimacy and effectiveness of its tax system. In other words, fair and effective taxation is a basic prerequisite for ensuring the stability over time of any political order. This is so because taxes ensure

¹¹ On the market as a social and economic institution, see Charles E. Lindblom, *The Market System*, New Haven and London: Yale University Press, 2001.

¹² Citizens can also owe to each other services in kind, such as the military or the civil service.

¹³ Cf. Ross Zucker, *Democratic Distributive Justice*, Cambridge: Cambridge University Press, 2002. See also Stephen Holmes and Cass Sunstein, *The Cost of Rights*, New York: Norton, 1999; Thomas Nagel and Liam Murphy, *The Myth of Ownership*, Oxford: Oxford University Press, 2002.

¹⁴ I have argued this *in extenso* in *Justifying Taxes*, *supra*, note 7.

that the socio-economic order guarantees the protection of fundamental rights to all citizens, independently of how well they fare in profit-seeking activities, by means of ensuring a baseline access to goods and services as well as a share of the general economic wealth (a characteristic of 'mixed economies' inherent in the welfare state paradigm).¹⁵ Secondly, public officials have levers to ensure the macro-economic stability of the socio-economic order and its effectiveness in realising key political and economic goals, such as sustainable development, full employment and price stability, that is, by means of providing regulatory tools, which allow authorities to reach certain macro-economic objectives.¹⁶ Taxes are indeed the price of civilisation.

Besides the general connection between taxes and democratic government, the Europeanisation of national tax systems has been one of the key processes in European integration. However, the contrary assumption is not only frequent, but typical. Indeed, it is usually assumed and believed that the process of European integration has not affected national tax systems and that taxation remains one of the few strongholds of national sovereignty.¹⁷ The fact that the

¹⁵ On the insurance logic of the welfare state, see Richard Titmuss, 'Welfare State and Welfare Society', in *Commitment to Welfare*, London: George Allen and Unwin, 1968, pp. 124-37. On the historical dimensions of the welfare state, see Douglas E. Ashford, *The Emergence of Welfare States*, Oxford: Basil Blackwell, 1986; Abraham de Swaan, *In care of the state*, Oxford: Blackwell, 1988; Clem Brooks and Jeff Manza, *Why Welfare States Persist: The Importance of Public Opinion in Democracies*, Chicago: Chicago University Press, 2007.

¹⁶ This is a rephrasing of the still canonical views on the role of public finance. See Richard Abel Musgrave, *The Theory of Public Finance*, New York: McGraw-Hill, 1959.

¹⁷ 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, *European Tax Law*, London: Kluwer Law International, 1997, at p. 3: '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* hardly exists as such. There is no tax levied at

assumption is widespread does not render it less wrong,¹⁸ for at least four reasons.

Community level by a Community tax authority'. We can find statements of national politicians repeating the same core idea. Consider for instance 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', CONV 782/03, available at <http://register.consilium.eu.int/pdf/en/03/cv00/cv00782en03.pdf>, where it can be read: 'We believe 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 of the Slovak Christian Democratic Party on tax sovereignty (June 2007), which (wrongly) claims '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', 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', 15 November 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'.

¹⁸ Susanne Uhl, 'Time for a Tea Party? Why tax regimes beyond the nation state matter, and why citizens should care, 14 (2006) *European Review*, pp. 565–85.

First, the kind of integration foreseen in the constitutive Treaties of the European Union, and actually realised in the last fifty years,¹⁹ could not have been achieved without a major transfer of taxing competences away from the Member States, and to the European Union (and to a certain extent, to supranational non-public or non-political collective decision-making processes, mainly the agents operating in financial markets). Indeed, the creation of a common, later single, market required redrawing economic borders, tearing down borders sheltering national economic agents from competition from other Member States and erecting new ones demarcating the Union. Given that tax systems play a paramount role in defining and sustaining economic boundaries,²⁰ the common market could not but require

¹⁹ 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. 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 productivity, but also make the widespread recognition of the citizens of all other Member States as members of the same political and economic community possible, thus nurturing the kind of we-feelings and solidaristic predispositions characteristic of modern democratic welfare states. 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 the 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 the projects which aimed at the direct and immediate establishment of a European federation (as European federalists advocated, and succeed in inscribing in the - failed - Military and Political Union of 1954).

²⁰ The geographical scope within which economic activity unfolds is still dependent on natural factors, such as distance, easiness and cheapness of transportation of goods or service providers. But as the technology develops, more economic borders are drawn mainly and almost exclusively by legal norms. The laws defining technical and safety standards play a key role in determining whether goods and services from third countries will be prevented

that substantial taxing powers were transferred to the Union.²¹ Indeed, the transfer of most powers related to customs duties,²² and several of those related to sales taxation was explicitly agreed in the founding Treaties of the Communities. As will be investigated in more detail in the third paper in this series, success in the achievement of the basic objectives of the Common Market fed a new round of claims to transfer bits and pieces of the powers concerning the design and collection of taxes bearing on capital, or even personal income.²³

Second, European integration has dramatically altered the nature of the taxing powers retained by Member States. The taxing powers are no longer exercised as sovereign powers of sovereign states, but as competences of Member States of the European Union, and consequently, subject to the European constitutional principles against which the validity of any norm, be it European or national, is to be determined.²⁴ This accounts for the growing

from competing in the home market. However, it is hard to contest that taxes play the decisive role in creating and recreating economic boundaries. Not only may customs duties be levied on the border, but there may be internal taxes applicable and restricted to foreign goods, services or even people, so as to discourage their entry into the national market. At the same time, national products that are exported may be entitled to tax refunds through which governments may camouflage subsidies hoping to boost the competitive position of companies established in their territory.

²¹ This was something unnoticed by most, but not all commentators 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, at 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'.

²² 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/London: Stevens and Sons, 1950. See also Bela A. Belassa, *Trade liberalization among industrial countries, objectives and alternatives* New York: McGraw Hill, 1967.

²³ 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 spillover argument is the background of the key Neumark report of 1962, see Rapport du Comité Fiscal et Financier, available at http://bookshop.europa.eu/eubookshop/FileCache/PUBPDF/CB6208070FRC/CB6208070FRC_002.pdf.

²⁴ The synthetic nature of European constitutional law renders the distinction between European and national constitutional standards analytically useful but substantively

jurisprudence of the European Court of Justice (and many national courts following suit of the judges sitting in Luxembourg), which has revealed the supranational constitutional limits to the taxing competences of Member States.²⁵

Third, European integration has led to sweeping changes not only in the legal framework governing national tax systems, but also in the economic consequences of national tax systems. On the one hand, the relative weight of different taxes has changed over time, and European integration is among the factors leading to such transformations. Value added tax (VAT) has become the sale taxation, as it not only enhances the transparency of cross-border transactions (in particular, concerning the 'transitory' practice of equalising charges) but also because it constitutes an adequate own resource of the Communities. Similarly, the significant shift away from capital taxation results from the way in which free movement of capital has been understood and applied since the 1988 Directive which established the principle of *erga omnes* free movement of capital as part of the single market package.²⁶ On the other hand, the process of European integration has considerably altered the degree of realisation of constitutional tax principles. The implementation of the four economic freedoms 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.

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 conflictos constitucionales europeos', 24 *Anuario de Filosofía del Derecho*, forthcoming.

²⁵ This is clear from a series of related judgments, the most important being 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'. Both the AG and the Court answered the question affirmatively.

²⁶ Directive 88/361 of 24 June 1988, OJ L 178, of 8 July 1988, pp. 5-18.

Fourth, European integration has affected the *stabilisers* of national democratic taxation, that is, the mechanisms which ensure that citizens are willing to comply *spontaneously* with their tax obligations without coercion. The tax systems of the Member States were built, or rebuilt in the post-war era, on the assumption that the community of economic risk – the space within which markets operated and the factors of production circulated freely – and the community of social insurance – the welfare state which insured citizens against economic risks – overlapped, as they were both national. The nation state, the national market and the national welfare state could reinforce each other if properly mediated by the right national tax system. Whether the national identity was a thick one based on a pre-political understanding of a common ‘fate’ rooted in a common history, language and culture, or a thin one based on the mutual recognition of citizens as holders of fundamental rights, collective identity could well play the role as a stabiliser of democratic taxation. This was so because identity motivated citizens to pay taxes independently of how much they would benefit from the welfare state. At the same time, the progressive diffusion of the belief that the welfare state did in fact deliver the goods, that it was closely related to the economic welfare experienced by Europeans in the post-war period, resulted in an additional stabilising factor (which following the usual terminology, we could say consisted in one form of output legitimacy). It was perhaps unavoidable that the process of European integration affected both stabilising factors. By redefining the community of economic risk, by means of removing or at least eroding national economic borders, it disrupted the correlation between the nation state, the national market and the national welfare state which had been the basis of the legitimacy of European states since the end of World War II.²⁷ Whether such stabilising factors could be adapted to supranational integration remains to be seen.

These four reasons ground the claims that: (1) European integration has been rendered possible by a major reallocation of taxing powers away from the Member States and towards the European Union; (2) integration has resulted in the narrowing down of the choice of nation states regarding the shape of their national tax systems; and (3) integration has altered the economic consequences of national tax systems, even the parts which had remained formally unaffected by European law.

²⁷ As the calls for a social Europe reveal.

The theoretical framework: Applying the RECON models to the tax policy of the European Union

In the first section of this paper I have explained why anyone interested in the democratic legitimacy of the European political order should have a close look at the processes of Europeanisation of national tax systems. The second item on the agenda of this paper is the specification of the three RECON models in the area of taxation.

The RECON models: The general theoretical framework and applied research

The RECON project revolves around three models of the European Union: the 'functional', the 'federal' and the 'cosmopolitan'. Each model has three dimensions: it may be regarded as a description of what the European Union is (*descriptive*), as an interpretative framework to reconstruct how the process of European integration has proceeded (*reconstructive*), and a normative yardstick against which to measure the legitimacy of the European Union (*normative*).

Moreover, RECON aims at spelling out institutional and policy reforms for each model. The project thus strives to connect each model with a specific democratising strategy which could bring the European Union closer to the (respective) normative ideal. Thus the distinction of 'renationalizing', 'federalizing' and 'cosmopolitan' reform strategies.²⁸ Similarly, RECON combines a theoretical reflection on democracy in the European Union (paying special attention to the specific problems which arise in a complex political order such as the one in Europe) with the application of the theoretical blueprint to specific policy areas. The aim of the project is to contribute to render each model more tangible by means of exploring its implications in

²⁸ See Erik Oddvar Eriksen and John Erik Fossum, 'Europe in Transition: How to Reconstitute Democracy', RECON Online Working Paper 2007/1, available at http://www.reconproject.eu/main.php/RECON_wp_0701.pdf?fileitem=5456091 and 'A Done Deal? The EU's Legitimacy Conundrum Revisited', RECON Online Working Paper 2007/16, available at http://www.reconproject.eu/main.php/RECON_wp_0716.pdf?fileitem=16662534.

concrete policy areas, as well as to identify the content of each model's reform blueprints.

On such a basis, the general theoretical framework of RECON needs to be specified for the tax field. This can be done by reference to four specific indicators, which serve to differentiate each of the three models on tax matters. This will be done in the following. I will proceed by first describing each of these indicators and the leading alternatives in their regard, and second summarising the implications of each of the three RECON models for the tax field.

The indicators

This paper (as in general in RECON work package 7 on the Political Economy of the European Union) will consider four sets of indicators: (1) the purpose of economic integration (in shorthand, the common market model); (2) the purpose of the specific socio-economic institution considered, in this case, the tax system; (3) the decision-making procedures, which cover the question of which procedures are carriers of democratic legitimacy and of which principles govern relationships between such procedures; and (4) the substantive elements which ensure the stability of the socio-economic institution, in this case, the tax system, over time.

The purpose of economic integration

The key means through which European integration has proceeded has indeed been economic integration. In particular, the three founding Treaties of the European Communities set as their purpose the creation of common markets through the establishment of a set of institutional structures and decision-making procedures, with the main purpose to realise the famous four economic freedoms (and free and undistorted competition) in their respective areas. It is telling that the European institutional framework has until recently been referred to as the 'common market', and that most legal and political analyses have tended to concentrate on the economic aspects of the integration process. Still, there are two rather contrasting conceptions of the purpose of economic integration, which are labelled here as the 'self-contained single market' and the 'embedded market'.

The 'self-contained' conception of economic integration assumes that the founding Treaties of the Communities enshrined a transcendental definition of the 'single market', the validity of which is a precondition of democratic

legitimacy, and not the reverse. The 'self-contained' conception of the common market amounts to an updated version of Lockean constitutionalism, with the four economic freedoms playing the starring role assigned to the right of private property in the older versions of the theory. In this reading, the Treaties identify the four economic freedoms as the core substantive content of the European socio-economic constitution, as the necessary guarantees of private autonomy, and consequently, of the respect of the individual preferences of citizens, of their realisation without any kind of coercion or force other than the one deriving from the limited character of economic resources and the actual cost of life plans. As a consequence, this conception overemphasizes the limits set upon legislators (both European and national) by the four economic freedoms. It is for this reason that it is closely associated with 'negative' integration, that is, with the active overruling of European and national norms which, in one way or the other, set limits to market freedoms.

The 'embedded' conception of economic integration presupposes that the economic sphere is but a part of the overall social order. Thus, its legitimacy cannot be established by exclusive reference to its substantive qualities, but depends on the legitimacy of the political order (thus the idea of 'embeddedness'). Setting economic integration as the goal of European integration therefore necessarily implies a program of reform, which goes beyond economic regulations, and covers those aspects of social and political regulation which are necessary preconditions for the legitimacy of the economic order as a whole. In this reading, the creation of a single market implies recreating at the European scale the embeddedness of national markets, and thus requires not only a combination negative and positive integration, but also highlights the key importance of temporary and exceptional measures to shelter the socio-economic order from dangerous stress in the phases of adaptation.

The complex character of the European political order allows for some to claim that 'economic integration' at the national level must be structured around the embedding of market institutions, while at the supranational level the only option is to establish a 'self-contained' market. One line of defence of such a position could be that the 'embedding' of the market calls for a decision-making process carrier of democratic legitimacy, which would simply not be available at the supranational level. It still remains to be seen whether the inner logic of a supranational self-contained market will not render impossible to sustain the 'embedded' market at the national level.

Table 1: Purpose of economic integration

Self-contained market	Embedded market
Affirmation of negative constitutional principles at the supranational level (the four economic freedoms) which allows realising private autonomy by checking the exercise of regulatory powers at all levels of government	Simultaneous establishment at the European level of the regulatory framework characteristic of an internal market and of the social and political institutions in which economic activities are embedded, and which constitute a precondition of market stability and efficiency

The purpose of tax systems

The purpose of taxation corresponds to the societal role(s) which the tax system is expected to discharge. Economic literature distinguishes three tasks that can be potentially assigned to the tax system, namely: (1) the funding of public goods and services, technically defined by reference to their non-rival and non-exclusionary consumption (*taxes as prices*);²⁹ (2) the funding of public goods and services, normatively defined by reference to a conception of distributive justice, and serving the purpose of correcting the allocation of economic resources resulting from the operation of market forces (excluded under option one) (*taxes as insurance premia*); and (3) the management of economic activity with a view to realise societal objectives such as sustainable growth, full employment, economic, monetary and price stability, or even balance of payments (*taxes as macro-economic tools*).³⁰ Each of these conceptions of the purpose of the tax system is characterised by a particular set of tasks assigned to the system.

Although there are several potential combinations, actual discourses on taxes revolve around two main variants. Firstly, *liberist* conceptions of taxation claim that taxes should first and foremost serve to fund public goods and services, understood in a technical sense, and consequently, serve as proxies of prices in the absence of conditions under which these are set by supply and demand.

²⁹ A standard definition can be found in Paul A. Samuelson and William D. Nordhaus, *Economics*, New York: McGraw-Hill, 1998 (16th edition), at p. 36: 'Public goods are commodities for which the cost of extending the service to an additional person is zero and which it is impossible to exclude individuals from enjoying'.

³⁰ The classical locus is Richard A. Musgrave, *The Theory of Public Finance*, New York: McGraw Hill, 1959.

Liberists only reluctantly admit the use of taxes with a redistributive purpose,³¹ and most (or at least, the most consistent ones) also oppose the use of taxes as macro-economic tools. The second variant is the *liberal* conception, according to which the tax system should fund public goods and services, including those intended to ensure a level of justice in the distribution of economic resources, and it should be a major lever in the conduct of macro-economic policy.

In complex and interlocking political orders, the analysis of the purpose of tax systems is complicated by the fact that one may advocate differentiated tasks for the subsystems at each level of government. One may hold that certain tasks should be reserved to, or interdicted from, the tax subsystems. As a consequence, it is proper and convenient to distinguish the question of the purpose of the *European tax system* as a whole, and the purpose of the *European, national and regional tax subsystems*.

Given the very limited role assigned to tax systems under the liberist view, those supporting such a model tend to pursue the confinement of all taxing powers (European, national and regional ones) to the establishment of taxes capable of funding what are public goods and services in a strict economic sense. This makes a very strong case for assigning strong negative constitutional taxing powers to the European level of government, as the more encompassing one, in order to establish the basic principles framing the exercise of legislative and collecting taxing powers. As will be discussed in more detail when considering the substantive elements of taxation, it is still the case that if limited and exceptional redistributive taxation would be undertaken, liberist (at least contemporary ones) would prefer to see it occur

³¹ Although the degree of opposition is variable. It was rather mitigated in Henry C. Simons, *A Positive Program for Laissez-Faire: Some proposals for a liberal economic policy*, Chicago: Chicago University Press, 1934 (advocating a quite comprehensive redistribution of economic resources); and even in the first Friedrich Hayek, as in *The Road to Serfdom*, London: Routledge, Kegan and Paul, 1944, where the state was expected to establish a social safety net. The standing of both authors as liberists is however contested among those following Ludwig von Mises' tradition. See Walter Block, 'Henry Simons is not a supporter of Free Enterprise', 16 (2002) *Journal of Libertarian Studies*, pp. 3-36 and 'Hayek's Road to Serfdom' 12 (1996) *Journal of Libertarian Studies*, pp. 327-50. See also Daniel Coldwell III, 'The Compatibility of Laissez Faire with Distributive Justice', 38 (1979) *American Journal of Economics and Sociology*, pp. 309-18.

at the more local levels of government. Thus one could conclude that liberist conceptions support a system in which the European and maybe even the national levels of government are precluded from using the tax system for redistributive purposes, while the interdiction is weaker at the local level.

The liberal model of taxation accommodates two contrasting views, depending on whether the European tax subsystem is charged with the task of funding the redistribution of economic resources. Some may argue, in line with the 'classical' fiscal federalism, that redistribution of economic resources should take place at the more encompassing level of government, as indeed seems to be required if the purpose is to ensure equality among European citizens qua European citizens. This comes hand in hand with the claim that macro-economic management through taxation should mainly correspond to the European level of government, given that the crucial taxes in this regard are those with a clear redistributive potential (i.e. personal and corporate income taxation). But others may argue, for a variety of reasons discussed in the literature of the 'new' fiscal federalism - including the insufficient democratic legitimacy of decision-making procedures at the supranational level, that redistributive taxation should take place only at the national and regional levels of government. This entails that macro-economic management through taxation needs to be undertaken through some form of coordination of national tax policies. Indeed, the use of taxes as a lever of macro-economic policy can only be effective within an integrated economic area if orchestrated at the highest level of government. Still, the assignment of the competence to shape redistributive taxes to national and regional governments requires an alternative to the direct discharge of such a task by the supranational level of government, which can only be coordination.

Table 2: Purpose of the European tax system

Liberist	Liberal	
	Supranational	National
All tax subsystems should aim at raising the funds needed to pay for public goods in a strict sense (non-rival, non-exclusionary consumption).	All tax subsystems should aim at raising the funds needed to pay for those goods and services which should be publicly provided, and they could be used as levers of macro-economic policy. There is a strong presumption in favour of discharging redistributive and macro-economic tasks through the supranational tax system.	National and regional tax subsystems should aim at raising the funds needed to pay for those goods and services which should be publicly provided. There is a strong presumption against the discharge of redistributive tasks through the supranational tax systems. Macro-economic management through taxation should be conducted through the supranational coordination of national tax systems.

Decision-making procedures in the tax field

Decision-making on tax matters concerns the procedures through which a democratic will is forged and put into practice. Three questions are important in this regard: (1) the sets of procedures and institutional actors which are part and parcel of the overall tax decision-making processes; (2) the principles governing the relationship between different decision-making procedures; and (3) the relationship between the different procedures.

A proper analytical framework that allows us to capture the plurality of powers exerted in the forging of a tax system must first be established. Although sometimes insufficiently stressed,³² the levying of any tax money is the result of a process defined in at least three differentiated steps, corresponding to three different aspects of the power to tax:

- The constitutional framing of the tax system; or the definition of the procedural and substantive principles according to which taxes should be collected, some of which are the general constitutional principles

³² The power to tax tends to be reduced to the power to levy concrete tax claims, i.e. to ‘cash in’ taxes. Indeed that is at the source of the claim that European integration has barely affected national tax systems (see p. 4 above).

governing the use of public power, while others are specific to the exercise of taxing powers (e.g. the principle of progressiveness of the distribution of the tax burden);

- The legislative definition of each concrete tax figure; or the power through which each tax figure is defined, specifying the elements needed to calculate the concrete tax liability of taxpayers and the variables relevant for the effective collection of taxes;³³
- The administrative collection of each specific tax debt, either on the basis of self-assessments submitted by taxpayers or assessments made by tax authorities; this power usually comes hand in hand with that to monitor compliance with tax obligations.

In a complex political order, such dimensions of the power to tax are normally not only differentiated in legal and political terms, but each power is trusted to different decision-making processes (and in federal or quasi-federal states, to different levels of government). Moreover, the lines of allocation of such powers may vary depending on the concrete tax figure in consideration. The common claim that the third dimension is the one where most power is wielded (which would justify the tendency to collapse the power to tax with the power to collect a specific tax) is thus inaccurate. Certainly, 'cashing in' taxes leads to empowerment through the actual control of economic resources (even if there is a legal mandate to transfer them to another level of government or to employ them in very specific ways), however, the first and second dimensions lead to empowerment to the extent that they limit, and can eventually severely constrain, the exercise of the administrative, 'cashing-in' power, and thus result in the assignment of structural influence on the shape of the tax system.

³³ Typically, the regulatory framework of each tax figure is established in two steps. Legislative procedures are employed to define the core elements of each tax (the tax base, the tax rate and the elements defining the spatial and temporal variables of the tax), while details are turned into concrete rules by means of regulatory procedures enshrined in statutory instruments typically authored by executive organs.

Table 3: The three powers to tax

Constitutional power to tax	Legislative power to tax	Collecting power to tax
Definition of the procedural and substantive principles according to which taxes should be collected	The power through which each tax figure is defined specifying the elements needed to calculate the concrete tax liability of taxpayers and the variables relevant for the effective collection of taxes	Administrative collection of each specific tax debt, either on the basis of self-assessments submitted by taxpayers or assessments made by the tax authorities; this power usually comes hand in hand with that to monitor compliance with tax obligations

As already hinted at when distinguishing three different aspects of the power to tax, there are good reasons why decision-making on tax matters takes places through a set of different and differentiated processes, in which a range of institutional actors participate.³⁴ In that regard, we can distinguish three main alternatives:

³⁴ The still frequent assumption that democracy requires the allocation of all legislative powers to a single institutional actor ('The Parliament') does not correspond (and never has corresponded) to the actual practice of any democratic state, and is moreover a poor alternative from a normative standpoint. Actual decision-making procedures are underpinned by the premise that democratic legitimacy can only be instilled on a decision if the decision-making process ensures a sufficient degree of participation and critical exchange of views, which calls for participation of a set of institutional actors other than Parliament. Even if the final decision takes place through a process of will-formation in Parliament, it has to be complemented by other processes to be legitimate (see for example Bruce Ackerman, 'The New Separation of Powers', 113 (2000) *Harvard Law Review*, pp. 633-729). Moreover, there are very good normative reasons why decision-making should be divided through the standard stages of constitution-making, law-making and act-making, captured by the analytical distinction between different dimensions of the power to tax. It must be said that by means of focusing primarily on procedures in which institutional actors participate rather than on institutional actors who decide through certain procedures, we avoid the risk of neglecting the actual power exercised by non-political and non-collective actors. Legal analysis of tax phenomena has indeed tended to ignore the constitutional assignment of negative tax powers to private actors and the exercise of tax powers through governance mechanisms. Due to the empirical correlation between wealth and capital income, the redistribution of economic resources depends on the ability to effectively tax capital income. It is important to note that the concrete mix of principles governing the distribution of tax powers *and* other key competences over the basic socio-economic structure of the political

Alternative 1: Decision-making is trusted exclusively to political and collective actors. This is the case when the constitutional design and practice is premised on the exercise of all three taxing powers by political institutions which are democratically accountable to individual citizens. This was the classical assumption of public law, which assumes a monopoly of the exercise of public powers by public actors. The model is not contradicted by the attempt of specific organised private actors to influence the shape of the tax system, provided that the constitutional setup does not result in the empowering of such actors. The determining factor here is that private actors can only have influence by persuading political actors that their own interests actually reflect the general will and interest of the community.

Alternative 2: Decision-making is trusted to both political and non-political collective actors. This is the case when the constitutional design and practice assumes a division of taxing competences between political institutions accountable to individual citizens and non-political institutions, acting either as agents of political institutions, in charge of a constitutionally established task fixed by the political institutions, but with a considerable degree of autonomy in the selection of means to carry out the specific task, or acting as

community may result in further limits to the 'overall' power to collect taxes in a given political community. In concrete, it may empower non-public procedures or actors to wield their influence and shape the exercise of tax powers, rendering *de facto* impossible tax decisions which are perfectly legitimate *de jure*. Consider the consequences which derive from a competence mix in which Member States have the competence to collect personal and corporate income taxes, and the institutionalized mechanisms to monitor compliance with such taxes remain exclusively national; but in which Member States are prevented from imposing any limit on the flow of capital to and from the state. This results in depriving any level of government from the power to effectively tax and monitor compliance in many cases, such as those organising their income flows around different Member States or third states, so as to render them opaque to national authorities whose informational basis remains basically national. See Thomas Piketty, *Les hauts revenus en France au XX^{ème} siècle Inégalités et redistributions, 1901-1998*, Paris: Grasset, 2001. This has been the case in the EU since the approval of the 1988 Directive on the movement of capital, which resulted in a structural limitation of the actual power to tax capital income, to the extent that such income can be rendered mobile. Similarly, consider the mix of competences according to which Member States remain competent to define and collect corporate income taxes, but are prevented from limiting the importation of goods or the provision of services from third countries as well as the decision of companies to transfer their seat to another jurisdiction. This also creates limits on the power to define the corporate income tax base and rates, at least vis-à-vis the companies whose threat to establish themselves in a third country is credible.

an alternative for establishing a general will combining the will of both public and private actors – as in the case of ‘multi-level’ governance.³⁵

Alternative 3: Decision-making is trusted to both political/collective actors and non-political/non-collective actors. This is the case when the constitutional design and practice assumes a division of taxing competences between political institutions which are accountable to individual citizens and private actors, acting either individually or as private factional organisations. This option is constitutionally entrenched when we find a combination of two or more of the following three structural principles: (a) ‘negative’ constitutional principles limiting the scope of public decision-making in tax matters; (b) a division of taxing competences between levels of government which favours the status quo rather than a change by means of multiple veto points; and (c) a strong power of constitutional review of tax legislation based on individual complaints to courts.

As was the case with the purpose of the tax system, the picture is complicated further by the co-existence of different tax subsystems, as it is perfectly possible that some of the variants are nuanced in a federal or multi-level context, by means of establishing a different range of institutional actors legitimated to intervene in tax decision-making at different levels of government. In particular, it is frequent to find alternative 2 concretised in the terms of assigning to political actors taxing powers *exclusively* at the national and regional levels, but considering that decision-making over the competences assigned to the supranational tax system should be exerted through governance mechanisms of one type or the other.

³⁵ Edoardo Chiti, *Le agenzie europee*, Padova: CEDAM, 2002.

Table 4: Democratic decision-making procedures in the tax field

Democratic government	Democratic government plus governance	Democratic government plus private decision-making
<p>Presupposes a clear allocation of powers across levels of government and within each level of government, and the ultimate steering of collective decision-making by representative institutions</p>	<p>Assumes that the political, social and economic complexity of a post-national polity requires that social integration takes place not only through ‘government procedures’ which lead to forging a single general will, but accommodates the co-existence of a plurality of common action norms through alternative ‘governance’ procedures, through which public actors find ways to accommodate unity and diversity (e.g. the open coordination method)</p>	<p>As in ‘democratic government plus governance’, assumes that social integration cannot be based on the forging of a single general will for the whole Union; alternative collective will-formation processes should include not only ‘governance procedures’ in which public actors interact in non-hierarchical ways, but also private decision-making (as for example in financial markets)</p>

The second dimension of tax decision-making concerns the relationship between the different decision-making processes in the tax field, and the principles governing the relationship between the tax norms produced through each decision-making process. Are the processes to be regarded as an overall attempt at defining a coherent democratic will on tax matters, or is the tax system to be the result of the uncontrolled overlap (and prospective conflict) between different tax decision-making procedures? How are we to conceive the roles of the norms produced through each decision-making process in the overall tax system, and to solve prospective conflicts? In this regard, there are two main alternatives, the second coming in three different shapes:

Alternative 1: *Tax competition*: It might be argued that the legitimacy of tax decision-making is enhanced by a strict separation of taxing powers between different decision-making processes, which excludes the establishment of clear principles governing the relationships between norms produced in different spheres of taxing competence. Taxing power being one of the core powers through which the state interferes with the right to private autonomy, there is a strong case for a constitutional framework which fosters competition between the different decision-making processes, as this is likely to reduce the

chances of taxing powers being exercised for other purposes than taking charge of the tasks assigned to the tax system.

Alternative 2: *Tax cooperation*: This alternative assumes that the division of taxing competences should come hand in hand with the establishment of structural principles governing the relationships between tax decision-making processes, so as to ensure the formation of a coherent and consistent overall tax system. There are three options:

- *Democratic government*, that is, division of competences and hierarchy; the latter acting as a standard criterion within each sphere of taxing competence, and as a residual principle of solving conflicts across spheres of taxing competence;
- *Democratic government supplemented by political effectiveness*, that is, the legal criteria (division of competences and hierarchy) may only help us solve part of the conflicts, as they would either not provide a clear solution to all conflicts, or there would be countervailing political reasons that would result in the setting aside of the legal solution in concrete cases. This calls for non-legal, political criteria to be negotiated and established case by case;
- *Democratic government supplemented by democratic governance*, that is, the legal criteria characteristic of democratic government (division of competences and hierarchy) must be supplemented by non-hierarchical, procedural principles, which provide solutions in cases in which standard democratic principles are either inconclusive or inoperative for political or economic reasons

Table 5: Principles governing the relationships between tax systems

Tax Competition	Tax Cooperation		
Conflicts are cleared by economic pressures stemming from the overlap of different tax decision-making processes	Division of taxing powers should come hand in hand with principles ensuring the formation of a consistent democratic tax will		
	<i>Democratic government:</i> Division of Competences and Hierarchy	<i>Democratic government supplemented by effectiveness:</i> Formal legal principles supplemented by economic and/or political negotiation	<i>Democratic government supplemented by democratic governance:</i> Formal legal principles beyond the division of competences and hierarchy; meta-conflicts to be solved through non-hierarchical principles, by the 'proceduralisation' of the meta-conflict

The stability of the tax systems

The final set of indicators corresponds to the stability of the tax system, and in particular to the substantive features of the societal order that render possible the establishment of an effective tax system, and that ensure its reproduction over time. Indeed, democratic decision-making in tax matters is only possible if most citizens are willing to voluntarily comply with their tax obligations.³⁶ Compliance cannot in the long run be sustained through coercion because complex modern tax systems require an active participation of citizens through the self-assessment of their tax obligations.³⁷ Propaganda is far from an attractive alternative, as it not only undermines the very basis of democratic legitimacy, preventing citizens from being critically reflexive about political decisions, but may also exhaust itself rapidly once an external shock results in the blatant contradiction of the 'official picture'. If coercion and

³⁶ At the same time, it has been observed that the fact that most citizens are willing to comply with their tax obligations without being forced to do so explains not only why democracies can impose higher tax burdens but also why the criteria for the allocation of taxes can be more complex and sophisticated. On this, see Douglass C. North, *Institutions, Institutional Change and Economic Performance*, Cambridge: Cambridge University Press, 1990, in particular Chapter 6.

³⁷ Personal and corporate income taxes, VAT and other sales taxes rely on the accurate self-assessment of citizens themselves, strategically and not exhaustively monitored by tax authorities.

propaganda are out of question, the mere fact that a general law prescribes citizens to pay a tax may not be sufficient to ensure compliance. The predisposition to pay taxes that have been decided democratically needs to be further supplemented by some form of collective identity. In that regard, there are three main types of identity relevant for our present purposes:

Alternative 1: *An interest-based identity*, that is, a post-political bond between fellow citizens, based on the persistence of common interests and the benefits derived from a given set of public goods and services. This collective identity results in solidaristic predispositions among strangers, modelled on the economic ideal of the free market; and what is shared is essentially speaking a market, i.e. a community of economic risks.

Alternative 2: *A thick communitarian identity*, that is, a pre-political bond between fellow citizens, based on the common possession of certain traits (language, historical memories, or even certain 'ethnic' commonalities) which nurtures a predisposition to sacrifice one's personal interest for the sake of the collective as a whole. This collective identity results in kinship-type solidaristic predispositions, modelled on the pre-political association *par excellence* – the family. This presupposes that what is shared is both a community of economic risks and a community of insurance in which affiliation is based on pre-political traits.

Alternative 3: *A thin civic identity*, that is, a political bond between fellow citizens, which nurtures a predisposition to act in such a way as to acknowledge others as holders of fundamental rights and duties, and consequently, as potentially entitled to require the sacrifice of personal interest for the sake of the interest of other citizens. This collective identity results in solidaristic predispositions among strangers, modelled on the political ideal of friendship. This presupposes that citizens share both a community of economic risks and a community of insurance in which affiliation is based on political traits.

The federal structure of the European political order introduces a higher degree of complexity, given that it is possible to claim either that all subsystems are stabilised by the same form or by different types of collective identity. In particular, it is frequently argued that while the national tax subsystems are stabilised by a civic or a communitarian collective identity, which goes hand in hand with contemplating robust tasks for such

subsystems, the supranational tax subsystem is exclusively stabilised by an interest-based identity.

Table 6: Solidarity and the stability of the tax system

Mutual interest-based solidarity	Thick collective identity	Civic collective identity
The predisposition to act in accordance with solidaristic obligations is based on the interest of all citizens in the reproduction of the overall institutional order and the continued provision of a given set of public goods.	The predisposition to act in accordance with solidaristic obligations derives from a pre-political identity which citizens acquire in the educational process (in the case of 'born' citizens) or through socialisation (for 'naturalised' citizens and long-term residents).	The predisposition to act in accordance with solidaristic obligations is anchored in the mutual acknowledgment of rights and duties within a given political community. The reproduction over time of a polity of such features entrenches a sense of fairness which prevents defection on a narrow-interest basis.

The three models and their variants

Having defined the four indicators with the help of which we can concretise the three RECON models in the tax field, it is time to undertake the latter task, and to determine how each model will define each indicator. In addition, I proceed to distinguish two variants of the two first models (the functional and the federal one) on the basis of substantive differences concerning the procedures of decision-making, which are carriers of democratic legitimacy, and of the conception of distributive justice. Such a distinction is necessary to avoid major confusion, in particular with regard to the federal model. While from the standpoint of the general RECON models anyone advocating the transfer of full-blown taxing powers to the European Union would be characterised as a 'federalist', it makes a considerable difference whether such a transfer is concretised in negative constitutional powers which limit the power to tax in general, or in positive constitutional powers aimed at ensuring redistribution of economic resources and macro-economic management on a European scale. While stressing the structural commonalities between the two positions, the two are so contrasting that there is a good case to take proper account of the differences in the modelling of specific applications to tax matters.

1) The functional understanding of European taxes and the renationalisation strategy

The functional model of European taxation defines economic integration as a process of transformation (i.e. Europeanisation) of the institutional structures through which markets are embedded in each society. As sovereign nation states have lost the capability to ensure such embedding by means of their autonomous action, they have to coordinate powers and act through supranational institutions. But because it is not possible to design supranational decision-making processes as carriers of democratic legitimacy, such legitimacy must stem from national decision-making processes. This latter assumption forms the basis for the emphasis on the 'renationalisation' of decision-making on tax matters, which however is to be rendered compatible, on the basis of the former premise regarding the loss of capabilities of sovereign states, with the maintenance of supranational institutions and decision-making processes.

The supranational tax system is essentially assigned the tasks of as 'liberist' tax system, that is, circumscribed to the provision of funds with which to cover the costs of European public goods and services in a technical sense. Both redistribution of economic resources and the macro-management of the economy are regarded as pertaining to the sphere of national democratic politics, and consequently, no substantive transfer of competences should take place in this field. At most, coordination (either covering technical aspects or premised on full voluntariness) should be facilitated by European institutions and decision-making processes. Consequently, the supranational tax system is stabilised by exclusive reference to the mutual interest of Member States in the provision of a limited set of public goods and services, which strengthen democratic decision-making on national political processes.

It is possible to distinguish two variants of the 'functional' model of European taxation by considering the specific means through which democratic legitimacy is transferred from national political processes to supranational decision-making procedures.

The first option is to design supranational decision-making processes so as to ensure that the European general will results from the aggregation of national general wills, thus ensuring that there is a proper 'transmission' of the national general will into the European one. This requires that national representatives of a specific national general will are part of the European decision-making process, and that they can oppose any decision which is contrary to such a will. The standard embodiment of 'indirect democratic legitimacy' is the way

in which the Council of Ministers takes decisions when subject to the condition of unanimity (which is the standard rule on tax matters). Each minister here acts as the spokesperson of the national parliament (even if the limited degree of parliamentary control might result in an executive drift), and can oppose any decision contrary to her or his mandate.

The second option is to design supranational decision-making process so as to ensure that the European general will results from the implementation of a constitutional mandate supported by the unanimous aggregation of national general wills, typically through an 'expert' agent, i.e. an agency. A political agreement is required to define an area of public policy in which it is preferable that decision-making is rather based on expertise or technical knowledge than on political choice, and to define the normative preferences which should guide the action of the agent. A mechanism of 'agency governance' is a central plank of the Arbitration Convention on transfer pricing. Associated enterprises operating in several Member States may be subject to double taxation of their profits if different states take different views on 'transfer prices', i.e. the price level of goods and services traded within the enterprise. In such cases, and if Member States do not find an agreement concerning the prices for the purpose of calculating corporate income taxation in each country, an 'advisory commission' is to be established with a mandate to fix such prices. The commission is composed by national representatives and, of key importance, by 'independent persons of standing', that is, by technical experts on corporate taxation.³⁸

2) The federal model and the federalising strategy

The federal model of European taxation defends both the assignment of the full range of taxing powers (constitutional, legislative and collecting) to the European Union, and the governing of such powers through procedures which are carriers of democratic legitimacy. It assumes that the breadth and scope of economic integration is bound to affect the configuration of national

³⁸ In each case, either the Member States agree on the nomination of the experts, or, if that is not an option, the experts are drawn by lot. The list of experts can be found at: http://ec.europa.eu/taxation_customs/resources/documents/taxation/company_tax/transfer_pricing/forum/16th_list_independent_persons.pdf.

tax systems so deeply as to render unavoidable the establishment of full-blown democratic structures at the supranational level.

However, while all federal models share the structural features just described, we can distinguish two contrasting variants by reference to how they conceptualise the process of economic integration, the purpose of taxes and the means for ensuring long-term stability of the tax system.

The first variant may be labelled as the 'liberist/federal' one. It assumes that economic integration is a self-contained process, aiming at the establishment of a supranational democratic order framed by a set of constitutional principles, which ensure the full realisation of private autonomy. Consequently, European, national and regional tax systems should be assigned the limited task of providing the means with which to fund the provision of public goods and services defined in narrow, technical terms. Supranational, national and regional decision-making processes should establish the set of taxes due, but in doing so they should be subject to mandatory 'negative' constitutional principles, corresponding to the four economic freedoms which are the backbone of European constitutional law. The relationships between the norms produced at each level should be governed in formal terms by the principles of division of competences and hierarchy characteristic of democratic government, but this will result in a healthy 'competition' across and between levels of government, which will further reinforce the checks upon legislators across all levels of government. As a result, tax systems will be stabilised by the interest of citizens in the goods and services funded through taxes, and also by a 'thick' identity at the regional and local levels of government, which establishes alternative means of integrating society in solidaristic ways other than the state imposition of taxes. Although the European Court of Justice has tended to stress the embedded character of market integration in the European Union, the growing body of its jurisprudence concerning direct taxation can be said to embrace a federal/liberist model of European taxation. It has resulted in a European review of the constitutionality of national laws by exclusive reference to the 'negative' constitutional principles embodied in the four economic freedoms (from which a transcendental conception of the common market is derived). The very limited practical implications of the ECJ's case law specifying unwritten exceptions to the four economic freedoms on the tax field, i.e. the 'coherence' of the tax system and the 'abuse' of economic freedoms, seem to confirm such a conclusion.

The second variant may be labelled the 'liberal/federal' one. It assumes that economic integration requires the establishment of 'market-embedding' institutions at the supranational level of government, that is, that markets cannot be properly and effectively integrated unless the social and political institutions in which they are embedded are also integrated. Consequently, the European system of taxation should be assigned the very same tasks that are normally assigned to the national and regional systems, and a new division of powers among them should be established, with a view to ensure that their concurrent and collaborative action results in the achievement of the substantive goals of each system. Such division of powers should take into account that both redistribution of economic resources and macro-management of the economy need to be (at least partially) conducted at the higher level of government in order to be effective. Moreover, a residual principle of primacy of supranational norms should be affirmed, as is indeed characteristic in federal orders. The 'liberal/federal' tax system needs to be underpinned by a civic collective identity, by means of which citizens come to acknowledge each other as sharing a political identity and are predisposed to be solidaristic with its co-citizens at all levels of government, and not only at the regional or local levels (thus, the type of solidarity characteristic of the 'liberal/federal' model is indeed solidarity among strangers). The 'liberal/federal' view is the one underpinning the regulation of customs duties – and perhaps even more clearly, agricultural duties which play the same role regarding agricultural products. This is so because such duties are regarded as a tool through which international trade is made compatible with the pursuit of specific policies (in the case of agricultural duties, the Common Agricultural Policy), and thus, as a means of 'embedding' the common market in specific social structures. Moreover, all taxing powers concerning such duties have been transferred to the European Union, and indeed the amounts levied are part of the 'own' resources of the Union. This also explains why customs and agricultural duties are the only tax figure where law-making is not subject to the condition of unanimous agreement between the members of the Council of Ministers.

3) The cosmopolitan model and the cosmopolitan turn of the European Union

Advocates of a 'cosmopolitan turn' of European taxation defend both the assignment of the full range of taxing powers (constitutional, legislative and collecting) to the European Union, and the governing of such powers through a mixture of procedures, some carriers of democratic legitimacy, others structured around the idea of democratic 'network' governance.

As for the federal model, the cosmopolitan model assumes that the breadth and scope of economic integration is bound to be so considerable as to affect the configuration of national tax systems in ways that will render unavoidable the establishment of full-blown democratic structures at the supranational level. Having said that, it also concurs with the functional understanding of European integration in the view that it may be impossible (or inadequate from a normative standpoint) to aim at the governing of supranational taxes through procedures as carriers of direct democratic legitimacy. However, instead of relying on indirect democratic legitimacy based on national decision-making processes, the cosmopolitan finds promise in procedures of supranational democratic *governance* as a supplement and alternative to supranational democratic *government*. Thus, cosmopolitans trust both in democratic government and in democratic governance, the latter being characterised by procedures of establishing a general will alternative to standard democratic ones. In particular, democratic governance does away with the traditional assumptions underpinning public law concerning the hierarchical relationship between actors and decision-making processes, thus resulting in flexible 'partnerships' through which stakeholders can participate in fleshing out common norms, and in the doing away with the 'hierarchical' and 'coercive' character of law. Cosmopolitan tax systems are then stabilised, as the 'liberal/federal' tax systems, by a civic collective identity, which grounds solidaristic obligations 'among strangers'.

A typical application of the 'cosmopolitan' model to European taxes can be found in the use of 'codes of conduct' as 'soft law' alternatives to hard-law directives and regulations. The classical example is the code of conduct on harmful corporate taxation. Given the persistent failure to eliminate national tax practices which distort competition through the issue of directives or regulations, Member States agreed to convey an expert group with the mandate of elucidating the most outrageous national provisions, and to voluntarily phase out the norms which will be singled out by the experts. This has been rightly considered as the first instance of application of the (now) more general 'open coordination method'.

Table 7: The RECON models applied to tax matters

	Renationalisation		Federal		Cosmopolitan Deliberative
	Governance	Indirect Democratic Legitimacy	Liberist	Liberal	
<i>Economic Integration</i>	Embedded	Embedded	Self-contained	Embedded	Embedded
<i>Tax System</i>	EURO: Liberist NATIONAL: Ecumenical	EURO: Liberist NATIONAL: Ecumenical	Liberist	Liberal	Liberal
<i>Carriers of Democratic Legitimacy</i>	National political orders plus constitutionally mandated supranational orders	National political orders plus constitutionally mandated supranational orders	All aggregative political process subject to constitutional framework	Deliberative decision-making process at all levels of government	Deliberative decision-making process, according to the government or the governance grammars
<i>Principles governing relationships</i>	Democratic Government and Democratic Governance	Democratic Government	Democratic Government	Democratic Government	Democratic Government and Democratic Governance
<i>Relationship between governments</i>	Constitutional Delegation	Constitutional Delegation	Competitive	Collaborative	Collaborative
<i>Stabilisers</i>	EURO: Mutual interest NATIONAL: Ecumenical	EURO: Mutual interest NATIONAL: Ecumenical	Mutual interest plus thick identity at the national/regional level	Civic identity (solidarity among strangers)	Civic identity (solidarity among strangers)

Conclusion

This paper has aimed at setting the basic analytical framework for the study of the Europeanisation of national tax systems and the progressive and steady emergence of a European tax order. In the first part, I made the case for making research on the evolution of tax systems under European integration a key part of the RECON project. Not only is there a particularly intense and

close relationship between the design of tax systems and democratic institutions and decision-making processes, but tax integration has played a key propelling role in European integration as a whole. To summarize, I simply claim No European democracy without European taxation. In the second part, I aimed at specifying the three RECON models, by means of offering a general reconstruction of the implications each of them will have. This is based on the distinction of several 'dimensions' specific to the socio-economic problematique, and grounded on the preliminary study of the arguments put forward by all parties to cases before the European Court of Justice. In brief, this paper intends to grant European taxation a *droit de cité* in the RECON project. The next two papers in the series will flesh out the RECON way of thinking about the European tax order.