
Chapter 1

General Introduction

1.1. Aim

The aim of this book is to establish a framework of a legal doctrine on EU law in the field of direct taxes. This is a rather traditional goal of legal studies, but this book makes an attempt to pursue it in an innovative manner. Although it is hard to “turn law into numbers” as Siems explains,¹ doctrinal legal research may nonetheless benefit from more empiricism through the use of quantitative methods,² even though not all original legal questions can be addressed in this way.³ The research in this book is a modest contribution to this broader debate.

We will see later in this book that EU law in the field of direct taxes essentially is a subfield of EU constitutional law. The large majority of legal norms in this area are derived directly from the Treaty on the Functioning of the European Union (TFEU) through judicial decision making by the Court of Justice of the European Union (CJEU). For this reason, the research aim is put in context by relating it to the seminal work of Von Bogdandy who defined a doctrine of principles on European constitutional law as a systematic exposition of its most essential legal norms.⁴ The aim of this book is, using Mackor’s definition of legal doctrine, to offer a description and a rational reconstruction of the legal order of EU law in the field of direct taxes.⁵

Section 1.3. will explain the research framework after the introduction to the research question of section 1.2. Following in this introductory chapter is a synopsis of the book in section 1.4. The limits of the research are mentioned in section 1.5., and section 1.6. gives further guidance to the reader.

When we ultimately want to arrive at a doctrine of EU law in the field of direct taxes, we need to distinguish at the least between the most important

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1. Siems (2011).
 2. *See generally* Heise (2002); Ulen (2002).
 3. Siems (2008).
 4. Von Bogdandy (2009); Von Bogdandy (2010); Von Bogdandy et al. (2006).
 5. Mackor (2012).

and less important legal norms. Also, we need to organize and give structure to those rules in a manner that is relevant to those rules. This exposition may be said to be systematic if the structure and organization of the individual legal norms give identity to them as a united whole.

Because the goal of a complete doctrine on EU law in the field of direct taxes in all its positive and normative aspects is beyond the scope of this book, the research will focus on building a framework. The book attempts to sketch the basic contours of the system of EU law in the field of direct taxes. This framework of a legal doctrine in this subject area is meaningful if it advances our rational understanding about the structure and organization of legal sources and norms in this field of EU law. In short, this book purports to research EU law in the field of direct taxes as a system and the research aims to describe its structure and organization. This goal can be restated in the central research question of this book.

1.2. Research question

The central research question of this book is: *What is the structure and organization of EU law in the field of direct taxes?*

The Oxford English Dictionary defines structure as “the mutual relation of the constituent parts or elements of a whole as determining its peculiar nature or character” and defines a structure as “an organized body or combination of mutually connected and dependent parts or elements”. Organization is defined as “the arrangement and coordination of parts into a systematic whole”.

This book looks at how the elements of EU law in the field of direct taxes are arranged by the relations between them and how this organization gives identity to EU law in the field of direct taxation as a whole; as a system. This presupposes that there is, at the least, a weak form of cohesion between the individual elements of this system. Also, we believe that the whole is larger than and different from the sum of its parts. It is not sufficient to know what combination of elements exists in a system, but it is equally important to understand how these elements cohere into a larger and distinct identity.

The prevailing opinion among regulators, academics and practitioners on EU law in the field of direct taxation is that it is a complex system and pro-

duces outcomes that are unpredictable.⁶ Thus, while not wishing to question the validity of that presupposition, it does have some important consequences for the manner in which we research this field and, consequently, the interpretation of the research question.

The distinction between complex and complicated should be stressed at this point. A system is complicated when it is composed of many elements or “things”.⁷ EU law in the field of direct taxes is complicated because it is composed of a multitude of legal provisions, judgments, rules, facts and opinions. It would be less complicated and easier to understand if we could reduce the number of those elements and variables for our consideration. Accordingly, the main approach in prior research on EU law in the field of direct taxes was to consider each judgment or rule first in isolation and, after we gained insight in each separate element, we compared those elements and related them in successively larger groups and slowly induced the system by further generalization. Many publications on European and international tax law apply such a reductionist approach and review a particular judgment, an individual rule or a specific legal provision.

However, the existence of a multitude of different elements and variables is not the key reason why EU law in the field of direct taxes is complex and produces unpredictable outcomes. The complexity of EU law in the field of direct taxes results from the linkages and interdependencies between those elements.⁸ In fact, they are “irreducibly intertwined”.⁹ Complexity in a system cannot be reduced, but we can advance our knowledge by researching its structure and organization.

If the system of law is reduced to a collection of individual judgments and individual rules and we assume that they are created under some form of centralized strategic planning of the Court – i.e. the Court may be held primarily accountable for the homogeneity of those elements – we gain insight into the Court’s reasoning in those judgments and the requirements and effects of the rules that it governs. However, this knowledge about the various elements is not necessarily insight about how they are linked as a collective whole.

Prior research has provided negative normative evaluations of the effectiveness of the Court’s strategic planning of the legal system, essentially

6. See section 1.3.

7. Miller & Page (2007) at 10.

8. Id., at 9.

9. Mitchell (2009) at 4. According to Miller & Page (2007) page 9: “Complicated worlds are reducible, complex ones are not”.

because the elements of that system were found to be heterogeneous and the relations between them could not be rationally reconstructed into a collective whole. The normative recommendation that followed was, of course, that the Court's control should be tempered for it is evidently not competent and strategic planning of the legal system through a democratic process of legislation would be preferable. In sum, the Court encroaches too much upon the national legislator's competence and its judgments adversely affect the traditional system of international taxation.

If we accept that the system of law cannot simply be reduced to individual rules and judgments, and given that the Court is not the only agent in the negative integration process,¹⁰ we may perhaps better understand the complexity of EU law in the field of direct taxation, given that complexity exists and persists. Instead of making a rational reconstruction of the relations between the elements in the system, would research not be more effective and insightful if we observed and studied those relations directly? This is what the research question asks us to do.

The research question presupposes that EU law in the field of direct taxes is a cohesive whole that is organized and structured in a complex system. This book wants to observe, describe and give a rational reconstruction of that organization and structure. The research question is for this reason academically relevant because the basic debate in prior research in this field is whether EU law in the field of direct taxes is a cohesive whole that is structured and organized in a legally relevant manner, or not.

1.3. Research framework

Prior research has approached the problem by qualitative legal analysis (methods of interpretation of the law) alone. This has resulted in an academic debate of dialectic arguments from which little agreement has emerged, and agreement has emerged only slowly. The status quo is aptly described by Farmer who spoke of a "bewildering array of concepts":

Over the last 20 years, the Court has responded case by case to a series of Member State arguments. The result is that we now have a somewhat bewildering array of concepts in the case law such as non-comparability of situations, territoriality, fiscal coherence, tax avoidance, balanced allocation of taxing powers, and so forth. It is perhaps time for the Court – or perhaps one

10. See generally Fligstein & Sweet (2002) on interlinking of social agents and the effects on institutionalization of European integration.

or more of the Court's Advocates General – to seek to rationalize such concepts and explain the relationship between them.¹¹

Graetz and Warren surmised the – rather pessimistic – conclusion that the Court has led itself into a “labyrinth of impossibility”.¹² Wattel argued that the case law is full of “red herrings”.¹³ Vermeend equated reading the Court's decisions in the field of direct taxation with reading “Alice in Wonderland” as early as in 1996.¹⁴ To keep up with these popular semantics, the research question may be restated as: *Is there order in the chaos of EU law in the field of direct taxes?*

In plain English, the departure from prior research is basically this.

Prior research has inferred the structure and organization of the system by inductive reasoning, while at the same time questioning its existence as a united whole, by researching individual judgments and rules. In other words, it reduced the system of EU law in the field of direct taxes to its sources and norms and it presumed that a more detailed and advanced knowledge of those individual elements resulted in a better understanding of the system as a whole.

This book deduces the structure and organization of the system from the system itself by researching it as a united whole and it describes the place and role of the judgments and rules within that system. The legal doctrine that emerges in this way in this book is more a doctrine about the system as such, and less a doctrine about its individual legal sources and norms. The qualitative analysis of individual cases is, for that reason, rather concise in this book. The intention is not to approach the Court's interpretation of EU law in its direct tax case law critically, but to work towards a positive legal theory about the system that emerges from the body of case law in the field of direct taxes. For that purpose we follow a research framework of complexity science.¹⁵ Mitchell defines this research field as:

An interdisciplinary field of research that seeks to explain how large numbers of relatively simple entities organize themselves, without the benefit of any central controller, into a collective whole that creates patterns, uses information, and, in some cases, evolves and learns.¹⁶

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11. Farmer (2007) at 44.
 12. Graetz & Warren (2006); Graetz & Warren (2012).
 13. Wattel (2004).
 14. Vermeend (1996).
 15. Miller & Page (2007); Mitchell (2009); Ruhl (2009).
 16. Mitchell (2009) at 4.

The study of complex systems and networks has pervaded all of science.¹⁷ The emerging field of computational social sciences analyses complex networks and leverages the current capacity to collect and analyse data on individual and group behaviour.¹⁸ A small but increasing body of literature in legal studies analyses law as a complex system.¹⁹ The general motivation for this strand of research is that the legal system shows all of the characteristics common to complex adaptive systems such as eco-systems.²⁰

The research framework of complexity science has theoretical implications for the way the structure and development of the law are viewed. Some important studies have approached the issues connected with the law as a complex system by researching the path-dependence of legal change,²¹ the application of chaos theory to legal evolution,²² and self-similarity within the structure of the legal system; its fractal nature.²³ In this book, we also draw from the recent advancements in networks science to study the legal system of choice in this book; EU law in the field of direct taxes.

The concept of emergence is central to complexity science. A complex system is a “system that exhibits nontrivial emergent and self-organizing behaviors”, according to Mitchell.²⁴ The general idea is that behaviour and interactions at the micro-level of individual agents lead to macro-level properties – patterns and structures – of the system as a whole. And, the central question in this field of research is consequently which processes and dynamics lead to emergent and self-organizing behaviour.²⁵ According to Miller and Page:

[E]mergence is that individual, localized behavior aggregates into global behavior that is, in some sense, disconnected from its origins. Such a disconnection implies that, within limits, the details of the local behaviour do not matter for the aggregate outcome.²⁶

Thus, the more precise reason why this book does not go into the details of the Court’s grounds of judgment of the individual rulings – at least in part II of this book – is that such details are not per definition decisive for

17. Strogatz (2001).

18. Lazer et al. (2009).

19. Jones (2009).

20. Ruhl (1996); Ruhl (2009).

21. Hathaway (2001).

22. Roe (1996).

23. Post & Eisen (2000).

24. Mitchell (2009) at 13.

25. Id.

26. Miller & Page (2007) at 44.

the structure and organization of the system of EU law in the field of direct taxation. A normative evaluation of and recommendation for the application and interpretation of EU law on a micro-level in individual cases do not have priority if the primary aim of the research is to advance the understanding of the overall system that the Court's rulings have established.

The research framework of complexity is closely related to theoretical jurisprudence of legal autopoiesis of Luhmann and Teubner.²⁷ This jurisprudence has also been applied by Prebble in the field of taxation research.²⁸ The jurisprudence of legal autopoiesis also adopts a systems perspective on the law and has in common with complexity theory that the law is not reduced to a collection of individual rules and social agents, but that it treats the law as an emergent of the interactions within the system ("law is communication"). What legal autopoiesis and complexity theory also share is that they both accept the existence and significance of dynamic and self-organizing processes. The systems not only exhibit emergence, but the emergent also is an organized complexity that is due to feedback that is introduced to the system as a result of interactions. The theory of law as an autopoietic system, which was adapted from sociology, has also connected to network and graph theory for purposes of empirical analysis.²⁹ This book continues on the perspective of complexity theory, specifically network science, and suffices with this mention of legal autopoiesis to give further context.

In short, this book contributes to the more general paradigm shift from a reductionist model of law to a complex adaptive systems model of law between order and chaos.³⁰ The specific methodology of the research design will be explained in later chapters.

1.4. Synopsis

This book is divided into four parts. Part I, which is this first chapter, gives the general introduction. Part II researches the breadth of the Court's case law in the field of direct taxes and part III provides an in-depth rational reconstruction of the balanced allocation of taxing powers and its relation with other justification grounds. Part IV presents the conclusions.

27. Luhmann (1989); Teubner (1993).

28. E.g. Hikaka & Prebble (2010); Prebble (2011).

29. Paterson & Teubner (1998).

30. *See* Bourcier & Clergue (1999); Ruhl (1996).

We will analyse how the body of CJEU case law on EU law in the field of direct taxes is structured and organized as a whole in part II. First, chapter 2 provides an analytical framework for this part by explaining the theoretical background to the process that we assume has driven the structure and organization of the body of case law and we describe the method of research. Second, chapter 3 will explore the properties of the case law by analysing aggregated metadata on the cases. Third, chapter 4 will analyse how the body of case law is structured and organized on various levels and scales. We will specifically examine whether there is structural cohesion in the body of case law and whether its organization is legally relevant. The main innovation of part II is that the research relies on a quantitative method called social network analysis to establish the structure and organization of the system and to define which legal sources and norms are to be considered most essential to the evolution of EU law in the field of direct taxes. In that respect, this approach differs greatly from prior research that has attempted to establish legal doctrine only by constructive qualitative legal analysis. The overall product of the research of part II is reported in annex A which gives a systematic overview of the most essential legal norm of EU law in the field of direct taxes.

We will limit our focus in part III and research the structure and organization of the law further by establishing the meaning of the legal norm “a balanced allocation of the power to impose taxes between the Member States”. It is proffered in prior research that the introduction of this norm marks a critical juncture in the evolution of the system of EU law in the field of direct taxes and is important for its overall structure and organization.

The main innovation here is that the chapters of part III exhaustively research the legal norm of a balanced allocation of taxing powers with the result that we give a robust and well defined meaning to it that is consistent with other legal norms that we identified in part II. After an introduction to the analytical framework in chapter 5, we first examine the Court’s interpretation of that norm as such in chapter 6. Then, chapter 7 continues with an analysis of the relations with other legal norms which are functionally equivalent in legal doctrine, i.e. also perform the role of justification. Thereafter, the balancing of freedom of movement and the balanced allocation as an overriding reason of public interest is reviewed further by specifically researching elements of proportionality in the balanced allocation of taxing powers in chapter 8. As a final step of research in this part, we revisit the reasoning and outcome in *Marks & Spencer* (C-446/03), which

is the original authority of this legal norm, and chapter 9 offers a revised interpretation of that case.

The various elements of the research are tied together in part IV in a general conclusion about the state of EU law in the field of direct taxation. The aim of the conclusion of chapter 10 is to give a concise summary of the specific findings of this book, to revisit the overarching research aim and question more generally and to surmise what the findings of the research imply as avenues for future research.

Parts II and III are relatively self-contained, which means that some Court cases are introduced twice in this book and a few points are repeated. This choice mainly contributes to the readability of the book.

Overall, the weight of discussion in part II is more on personal income taxes, whereas part III is focused on EU law in the field of corporation taxes. In line with the internal logic of the Court's case law, part II pays closer attention to the conception and existence of a restriction, because part III is aimed specifically at researching the content of justifications for tax restrictions on freedom of movement. This organization of themes was not a deliberate research design choice as such, but emerged naturally as the research progressed over time.³¹

1.5. Limits

Member States of the European Union remain competent to legislate in the field of direct taxation. Although the Union has adopted only a few directives in the field of direct taxes, it nevertheless exerts extensive regulatory control over national direct tax systems.³² The process of integration from which this control results is chiefly directed by the judicial supervision of the CJEU. Or, as Radaelli and Kramer put it, the single major factor of legal pressures in the field of direct taxes is the case law of the Court.³³ In contrast to national direct tax law which is codified in many Member States to high levels of complexity, the content of EU law in the field of direct taxation is thus almost exclusively based on case law. Consequently, EU law in the field of direct taxation evolves incrementally in a common law fashion,

31. In that context, we should disclose that the first draft of the text of part II was written when the research and draft for part III were largely completed.

32. Genschel & Jachtenfuchs (2011).

33. Radaelli & Kraemer (2008).

case by case, without superimposed codification or strategic legal planning by an EU legislator. This justifies limiting our research to case law only. The system of EU law in the field of direct taxes is a narrow conception and only represents the system embodied in the case law of the Court.

National judicial decisions are ignored in this book. The limited aim of giving outlines of a legal doctrine on EU law in a specific field neither requires, nor merits the discussion of those national decisions. Also, language is a constraint to the potential countries that we could include if we were to conceive the relevant body of case law in a much broader definition to include national decisions, despite Google Translate.³⁴ Furthermore, data collection for the purposes of our research would be significantly more cumbersome. On balance, we believe that the limitation to the case law of the Court is justified.

The focus of the research is on EU law as interpreted by the Court, and this requires analysing the application of rules to the facts as evidently understood by the Court, even if the Court's take on the facts or the national legal framework may be incomplete or inaccurate. Although it is a responsibility of the academic community to draw attention to the normative merits of the ruling in view of its particular consequences for the national legislation in the various EU Member States ("the outcome"), one first needs to acquire an understanding of the rule that has been applied to determine whether a fact of national law that has been missed or misinterpreted by the Court would be material for the outcome in the first place.

The aim of this book is to arrive at a systematic understanding of the role and function of the various judicial rules that apply and belong to the legal doctrine of EU law in the field of direct taxes. Moreover, the dissertation project by Douma has researched the normative merits of the outcomes of the rulings on EU law in the field of direct taxes.³⁵ The reduction of national sovereignty that was the combined result of the outcomes of the individual rulings has been the subject of Isenbaert's dissertation project.³⁶ Monsenego has focused specifically on the case law concerning the taxation of foreign income.³⁷ As stated above, this book applies a research framework that is fundamentally different from the approach in those studies. The research of this book is therefore limited to a positive legal research and

34. See <http://translate.google.com>.

35. Douma (2012b).

36. Isenbaert (2010).

37. Monsenego (2012).

we will only touch upon the merit or demerit of the Court's interpretation of the law on a tangent.

The following topics will only be touched upon briefly because they concern a normative discussion about the future direction of EU law in the field of direct taxation: most-favoured-nation treatment,³⁸ non-discriminatory tax restrictions,³⁹ and juridical double taxation.⁴⁰ Although comparative law approaches,⁴¹ economic neutrality benchmarks,⁴² or other extra-legal theoretical models,⁴³ may give much desired insight into potential normative evaluations and recommendations for these issues, all of that is not the topic of this book. We also do not wish to base our analysis on a traditional normative framework of tax policy. The important study of Lang and Englisch on the European legal tax order based on the principle of ability to pay is a prime example of such a tax-oriented principles-based approach.⁴⁴ This is also not the type of research that this book aims to report.

For example, the disadvantage of juridical double non-taxation was clearly held not to be contrary to EU law according to the Court's line of authority starting with *Kerckhaert and Morres* (C-513/04). For that reason, any discussion about the merit or demerit of the reasoning and outcome of that judgment is normative in nature and therefore does not fall within the scope of this research which is concerned primarily with a positive theory on the structure and organization of EU law in the field of direct taxes. The question whether and how the rule of *Kerckhaert and Morres* "fits" within this structure and organization is of course an obvious follow-up to the findings of this research.

1.6. Guidance to the reader

Since this book builds on prior research and because science is a collective effort, even if the research was done by a single person under supervision of another, this book uses a "we"-narrative instead of "I" throughout this book. Also, "we" refers to both the reader and the author and allows for a more engaging writing style than the "I"-narrative. All errors or omissions in this book are of course my own.

38. See section 4.3.5.3.3. on the ruling in *D.* (C-376/03).

39. See sections 3.6.2.2. and 4.3.5.5.2. on the *Säger/Kraus* formula.

40. See section 3.6.2.2.1.

41. Avi-Yonah et al. (2007); Mason (2008).

42. Mason & Knoll (2012).

43. Roxan (2000).

44. Lang & Englisch (2006).

This book was written with a reader in mind who is knowledgeable about the basics of EU law and taxation. The institutional framework of EU law will not be discussed, nor will we venture into general reviews about well known principles as supremacy, conferral of competences, subsidiarity, proportionality and direct effect. These principles are only explained shortly when relevant and it therefore suffices to refer to the usual textbooks.⁴⁵

This book makes a rather strict division between views on the object of research as analysed in prior research and the qualitative analysis of the case law. Prior research is used primarily to formulate the research questions. Prior research is therefore reviewed on the basis of the main contributions of several publications. It would be methodologically weak to use the same literature to answer those questions. All references to the literature are given in author-date short form in footnotes. The full reference is given in the list of references in the back matter of this book.

All cases of the CJEU are cited in short form and usually directly in the main text. References to a set of cases are however put in a footnote to enhance readability of the text. The case number is given when the case is mentioned for the first time in each chapter. Thereafter, only the short name is used. When a reference may be ambiguous – especially for cases pursuant to direct actions – the case number is also mentioned to avoid confusing the reader. The full references of cases of other courts are given in footnotes. This book includes a table of cases with full references. Full references to legislation other than the Treaties are exclusively given in footnotes. All references to the Treaties are to the current articles of the TEU and TFEU, and quotations have been adapted with the use of square brackets, unless the provision was no longer in force post-Lisbon. References to EU directives are to the instrument in force on 1 January 2012.

Some final words on the use of the word “Court” in this book complete this chapter. The institution CJEU is currently composed of the Court of Justice, the General Court and the Civil Service Tribunal. The capitalized word “Court” is, in this book, a short name for the Court of Justice of this institution. References to the other courts are made explicit by using the full name. The national court that made the reference to the Court in preliminary reference procedures is normally not identified and the wording “national court” is used, unless the context requires identification.

45. E.g. Barnard (2010); Craig & de Búrca (2008); Kapteyn et al. (2008); Tridimas (2006).