

Towards a Homogeneous EC Direct Tax Law

Assessment of the Member States' responses to ECJ's case law

INTRODUCTION

Income tax law in the various Member States of the European Union is rapidly evolving. Instead of seeing discrete national systems we find that a pan-European – and sophisticated – level playing field is developing, where the game no longer follows a single national set of rules. More and more studies are being devoted to the polycentric character of direct taxation, whose complexity is increasing with the number of new Member States.

Many citizens, scholars and legal practitioners are turning towards the European Court of Justice (ECJ) as the ultimate defender of taxpayers' Community rights, for better or worse. A large variety of opinions are being expressed in tax law reviews, or even in the national media of the Member States on the positive or negative consequences of the cases decided in Luxembourg.

However, one may wonder whether the decisions handed down by the ECJ *actually* do have any impact on Member States' direct tax laws. How have "old" Member States coped with their duty to enforce the fundamental freedoms as interpreted by the ECJ in the field of income tax law? Are these rights taken seriously? What is the scope and effect of cross-border tax judgments? Are they worth all the trouble?

There are no empirical studies to date gathering insiders' views on how far the process of European integration has come since 1986, when the first judgment dealing with the Four Freedoms in the field of direct tax law (*Avoir Fiscal* (270/83) was rendered. This book is the first step towards achieving a better insight in how Community case law is actually understood and implemented in some Member States. It presents a picture of Member States struggling with the burden of securing taxpayers EC fundamental rights.

Most of the authors contributing to this empirical study have followed the development of this case law from the very beginning. We want to share our experience and reflections in order to assess the progress (or harm) done in direct tax law in our Member States.

We are therefore proposing a trip across the European Union, in order to assess whether the EU Member States' direct tax landscapes have changed in accordance with the ECJ's case law in direct taxation.

1. THE SCOPE OF THE BOOK

"Towards a Homogeneous EC Direct Tax Law, An Assessment of the Member States' Responses to ECJ's Case Law" is an empirical study of the actual impact of the fundamental freedoms, interpreted by the ECJ, on EU and EEA Member States in the field of income taxation.

This book addresses two issues: firstly, do taxpayers within the EU have access to the Community legislation granting fundamental freedoms provided for in Arts. 18, 39, 42, 48 and 56 EC? Secondly, has the Community legislation been applied homogeneously within the EU in twenty years of ECJ's case law on direct taxation? In order to answer these two questions, tax experts (practitioners and academics) who are familiar with Community legislation have carried out an empirical study in a sample of countries, representative of an evolution in the field of direct taxation.

2. PURPOSE

The *main purpose* of this study is to investigate whether, and if so how, the ECJ's substantial case law in the field of direct tax law has had an actual impact on Member States' tax laws. The *secondary purpose* of this study is to present a comparison of Member States' reactions to the ECJ's rulings, mostly on behalf of the domestic judges whose duty it is to implement the fundamental freedoms provided for by the EC Treaty.

Ultimately, our project hopes to initiate a discussion about the ECJ's actual role in the uniform application of EC law in the field of direct taxation within each Member State. The underlying issue raised in this research touches upon the identification of problems in implementing EC tax law. In a first step we have tried to find out whether there was a problem at all, and therefore we focused on the "sick cases" and have discussed in our reports how Community rights arising from ECJ case law were treated in each Member State.

The focus on the effect of the ECJ's case law is, ultimately, an attempt to resolve some of the controversy surrounding the "binding force" of these cases. We are not interested in the uncontroversial binding force of EC law with "federative" effects - for example, regulations, or even directives granted direct effect, as they *must* be considered as binding sources of law in all circumstances (even if this is not really adequately taken into account by all domestic legislation).

This study is dedicated to sources of law such as ECJ case law (or even new "soft law" codes of conduct, for instance) or directives without direct effect, in order to look from *the perspective of domestic courts* at whether these sources *should* be taken into consideration in their decisions, or only *may* be taken into account. Further, we look at how these non-binding sources of law actually are implemented in domestic income tax laws.

The goal of this study consists ultimately of illustrating the paradox inherent to Community law: How to achieve a uniform application of Community law despite the diversity in Member States' direct tax laws?

3. METHOD

In order to decide whether Community law is being applied homogeneously within the European Union, it is adequate in the first place to know what kind of impact it has generated on Member States' tax law. This study is therefore based on a comparative law method, where domestic tax law experts familiar with the use of Community law in the field of direct taxation were asked to answer identical questions about the actual impact of the fundamental freedoms on their domestic tax rules.

Some basic assumptions had to be made in order to facilitate this comparison. Firstly, it seems fair to state that the implementation of Community law in the "old" Member States still is less than perfect, even after twenty years of ECJ case law condemning discriminatory and restrictive tax law provisions. Consequently, the study presupposes that some of the Member States' tax laws are still incompatible with Community law, due to the general attitude among domestic legislators (which ranges from ignorance to counteractive exaggerated measures as a reaction to an ECJ decision). In other words, **assumption one** is that the actual impact of the ECJ's case law is not as extensive as it should be.

Further, as a result of an erroneous and incomplete incorporation of Community rights in the field of direct tax law, domestic judges are put in a position where they have to supplement the deficiency of legislative power. How the domestic judges carry out this task is a central issue in the correct application of Community law, and also the ultimate place where taxpayers may claim their Community rights. Therefore, our investigation is initially directed towards domestic tax cases in which national tax law is questioned on the ground of the Treaty of Rome (or any other piece of Community legislation).

As a result, **assumption two** is that the most adequate way to measure the actual impact of ECJ case law on Member States' domestic tax law would be to analyse domestic judges' attitudes towards this source of Community law. Whereas the domestic cases leading to ECJ rulings (either on the basis of Art. 234 EC or on the basis of Art. 226 EC) are quite well known and have been extensively commented on, it seemed more interesting to focus on domestic courts' decisions in which no reference to the ECJ in Luxembourg was made, and which were not reported internationally.

Therefore, **assumption three** is that the actual impact of Community law also is seen in other places than in (or in addition to) the cases decided by the ECJ itself. However, it was also considered that there must be some cases where domestic courts should not be in a position to interpret the conformity of national tax law with Community Law, since a uniform interpretation of Community law would instead require an interpretation by the ECJ.

Therefore, **assumption four** is that domestic courts refer too few (or too many) cases to the ECJ on issues of interest to the entire Community. Consequently, the national reporters were also asked to check how Art. 234 EC was put into practice in their own tax jurisdiction.

Finally, the actual impact of Community law also had to be assessed as regards the legislator and the tax authorities' attitude. Indeed, a positive attitude towards the fundamental freedoms in the legislature might lead to fewer cases to be dealt with by domestic courts and would result in an actual effective application of Community law in the field of direct tax law.

Therefore, the reporters were also asked to report on whether the internal tax law was regularly amended and updated in order to cope with the ECJ's case law interpreting the EC Treaty. Although this book is not meant to provide a subjective judgment of value on the Member State's fidelity to Community legislation, it does compare the level of enforcement of taxpayers' rights in different Member States, while trying to identify problems faced by law-makers and judges in this mission.

In order to reach a common ground for comparison of Member States' reactions to the ECJ's case law, a questionnaire was designed, addressing two main issues. In a first series of questions, the reporters were asked to investigate whether the specific constitutional framework in their Member State would explain difficulties in implementing the ECJ's case law in their tax laws. These obstacles could range from a lack of recognition of the supremacy of EC law to problematical procedural rules, which may jeopardize taxpayers' access to their Fundamental Freedoms.

In a second series of questions, the reporters were asked to collect information mainly linked to direct tax law. The underlying idea in this comparative approach was to assess whether domestic law is actually evolving and implementing the fundamental freedoms.

For instance, both Swedish and Portuguese tax law provide for a roll-over of capital gains tax on permanent housing for individuals, provided that the taxpayer invests in new permanent housing within the same Member State. As early as 2003, Swedish taxpayers have challenged this exit taxation in court on the grounds of the ECJ case *de Lasteyrie* (C-5/02). Long before the Commission initiated proceedings against Sweden under Art. 226 EC, Swedish judges had started allowing (although not systematically) the roll-over of capital gains tax when taxpayers moved to another Member State. It was not until October 2006, however, that the Swedish tax legislator took the question seriously and started to legislate an amendment of the disputed tax provision.

So the reporters were asked to identify those areas of taxation where a potential or open conflict with Community law had occurred in domestic tax case law, and to assess whether these cases had contributed to a more effective application of Community rights for taxpayers. The areas targeted did not encompass restrictions, and the reporters could use any relevant income tax provision still in conflict with Community law.