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HOW IS EC TAX LEGISLATION MADE?

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EC tax legislation can take the form of directives, regulations, decisions or recommendations. A directive is a measure which is "binding, as to the result to be achieved, upon each Member State to which it is addressed", but it leaves "to the national authorities the choice of form and methods".[2] Typical examples of directives in the tax field are the various VAT directives,[3] the various excise duty directives,[4] the directives on capital duty,[5] the directive on the taxation of parent and subsidiary companies[6] and the directive on the taxation of mergers, divisions, transfers of assets and exchanges of shares.[7]

A regulation is a measure of general application which is binding in its entirety and directly applicable in all Member States.[8] In the fiscal area, regulations are used principally in the customs area because this is the sole fiscal area where the revenue goes direct to the Community budget.

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2 Article 249 EC, third paragraph.

3 Notably the Sixth VAT Directive 77/388/EEC, OJ L145, 13 June 1977, as last amended by Directive 1999/59/EC, OJ L 162, 26 June 1999, p.63.

4 See Council Directives 92/78/EEC to 92/84/EEC published in OJ L316, 31 October 1992, page 5 ff.

5 Council Directive 69/335/EEC concerning indirect taxes on the raising of capital (OJ L249, 3rd October 1969, p.25), as last amended by Directive 85/303/EEC, OJ L156, 15th June 1985, p.23.

6 Council Directive 90/435/EEC, OJ L225, 20th August 1990, p.6.

7 Council Directive 90/434/EEC, OJ L225, 20th August 1990, p.1.

8 Article 249 EC, second paragraph.

A decision is binding in its entirety upon those to whom it is addressed.[9] A typical example can be found in the various decisions taken by the Council or the Commission authorising Member States to derogate from certain provisions of the VAT or excise directives. Such decisions should be seen as secondary legislation adopted pursuant to powers conferred by directives.

Recommendations and opinions have no binding force; they merely exhort Member States to adopt certain conduct.[10] The legislative procedure for adopting a recommendation is shorter than that for adopting a directive or regulation. For this reason recommendations are sometimes used by the European Commission as a means of encouraging Member States to take certain action, failing which the Commission will introduce proposals for a formal directive or regulation.[11]

When it comes to taking measures at an EC level to avoid double taxation, the correct method of proceeding is by way of multilateral convention adopted pursuant to Article 293 EC. The sole example is the Convention setting up an arbitration procedure to avoid double taxation in connection with the adjustment of profits of associated companies.[12]

A final residual category concerns resolutions which are more in the nature of policy statements than legislation. A recent example is the Resolution of the Council and the Representatives of the Governments of the Member States on a code of conduct for business taxation.[13]

Primary EC fiscal legislation is adopted by the Council and must have, as its legal basis, an article of the EC Treaty. Secondary EC fiscal legislation is adopted by the Commission, or by the Council on a proposal from the Commission (without further consultation), pursuant to an enabling provision of primary legislation. Typical examples of secondary fiscal legislation can be found in the customs, VAT and

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9 Article 249 EC, fourth paragraph.

10 Article 249 EC, fifth paragraph.

11 For example, see Commission Recommendation on the taxation of certain income derived by individuals from a Member State other than that of their residence, OJ C121, 15th January 1994.

12 Convention 90/463/EEC, OJ L225, 20th August 1990, p.10.

13 Annexed to Conclusions of the Ecofin Council Meeting of 1st December 1997 concerning taxation policy, published in OJ C2, 6th January 1998, p.1.

excise area.[14] Failure to state the correct legal basis in the preamble to primary or secondary legislation is a ground for annulment by the Court of Justice. The principal legal bases and legislative procedures for primary fiscal legislation are examined below.

In relation to indirect taxation (VAT, excise duties) the principal enabling provision of the EC Treaty is Article 93 EC (formerly Article 99) which provides as follows:

> "The Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament and the Economic and Social Committee, adopt provisions for the harmonisation of legislation concerning turnover taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and the functioning of the internal market within the time limit laid down in Article 14."

Article 99, now Article 93 EC, was the legal basis used for the basic directive setting up the single market arrangements for excise duty.[15] The package of directives adopted on 19 October 1992 approximating excise duty rates was also adopted simply pursuant to Article 99 of the EC Treaty, now Article 93.[16]

In relation to direct taxation the principal enabling provision of the EC Treaty is Article 94 (formerly Article 100) which provides as follows:

> "The Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament and the Economic and Social Committee, issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the functioning of the common market."

Article 100 was the legal basis used for the two directives referred to above on the taxation of parent and subsidiary companies and on the taxation or mergers, etc.

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14 There are many examples, but the most recent are Council Decisions 2001/2453/EC and 2001/244/EC of 19th March 2001 published in OJ L88, 28th March 2001, pp. 15 and 17.

15 Council Directive 92/12/EEC on the general arrangements for products subject to excise duty and on the holding, movement and monitoring of such products, OJ L76, 23rd March 1992, p.1.

16 See Council Directives 92/78/EEC to 92/84/EEC published in OJ L316, 31st October 1992, page 5 ff.

Sometimes fiscal measures have been adopted on the basis of both Articles 99 and 100, now Articles 93 and 94 EC. This was the case notably for the Sixth VAT Directive and for the Directives on the taxation of the raising of capital. On the other hand, the amendment to the Sixth VAT Directive required to give effect to the single market was simply adopted pursuant to Article 99 of the EC Treaty, now Article 93.

As has already been observed, action taken at EC level to avoid double taxation should be regulated through multilateral convention. Article 293 EC (formerly Article 220) provides as follows:

> "Member States shall, in so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals:
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> - ...
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> - the abolition of double taxation with the Community;
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> - ..."

Then there is a catch-all enabling provision in Article 308 EC, formerly Article 235, which provides as follows:

> "If action by the Community should prove necessary to attain, in the course of the operation of the common market, one of the objectives of the Community and this Treaty has not provided the necessary powers, the Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament, take the appropriate measures."

In the customs area, the enabling provisions are twofold. Article 26 EC (formerly Article 28) provides as follows:

> "An autonomous alteration or suspension of duties in the Common Customs Tariff shall be decided by the Council acting by a qualified majority on a proposal from the Commission."

Article 133 EC (formerly Article 113) provides as follows:

> "The common commercial policy shall be based on uniform principles, particularly in regard to changes in tariff rates, the conclusion of tariff and trade agreements, the achievement of uniformity in measures of liberalisation, export policy and measures to protect trade such as those to

be taken in the event of dumping or subsidies."

"The Commission shall submit proposals to the Council for implementation of the common commercial policy."

The Community Customs Code was adopted as a Council Regulation pursuant to Articles 28, 100A and 113 of the EC Treaty, now Articles 26, 95 and 133.[17] This was because the Community Customs Code provides for autonomous tariff suspensions (Article 26 EC), for customs administration generally (Article 133 EC) and internal market measures (Article 95 EC). The Regulation was adopted after consulting the Economic and Social Committee and in co-operation with the Parliament pursuant to the procedure laid down by Article 189C of the EC Treaty, now Article 252 EC. If the same regulation had to be adopted today, the co-decision procedure pursuant to Article 251 EC, formerly Article 189B, would apply instead of the co-operation procedure.

It should be remembered that, in the case of agricultural products, import from a third country gives rise not only to liability for customs duties, but also to agricultural levies designed to support prices within the Community pursuant to the common agricultural policy. Like customs duties, agricultural levies are transferred directly to the Community budget. The principal enabling provision here is Article 37 EC (formerly Article 43). The day-to-day administration of agricultural levies is carried out by the Commission pursuant to powers delegated to it by the EU Council. This is a specialist area more appropriate to a study on the common agricultural policy. It is not generally considered as forming part of EC tax law and will not be examined further here.

From the foregoing articles, the three important characteristics of the legislative process can be distilled, in so far as they apply to fiscal legislation. First, unanimity is required among the Member States for the adoption of any primary EC measure in relation to direct or indirect taxation. The same is obviously the case also for the conclusion of a multilateral convention for the avoidance of double taxation. On the other hand, in the case of an autonomous[18] change in customs duties, and in the case of commercial policy measures, the Council acts by a qualified majority within the meaning of Article 205 EC (formerly Article 148), the Member States' votes being weighted in accordance with the provisions of that same Article.

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17 Council Regulation (EEC) No 2913/92, OJ L302, 19th October 1992, p.1.

18 I.e. a change in customs duties which is not governed by, or is not contrary to the EC's tariff commitments pursuant to GATT 1994.

The second striking characteristic of the legislative process is that no directive or regulation can be adopted by the Council in the fiscal area (or indeed, in any other area) unless the Commission takes the initiative and submits a proposal to the EU Council.[19] Moreover, for so long as the proposal has not been adopted as a final Community act, the Commission may alter or withdraw its proposal.[20]

The third characteristic is the fact that the Commission and the Council are not the only institutions having a say in the matter. In all matters concerning direct or indirect taxation adopted pursuant to Articles 93, 94 or 308, the Council is obliged to consult the Economic and Social Committee and also the Parliament before taking its final decision. It should be noted that, in fiscal matters, the Parliament is simply consulted. It has no role of "co-operation" or "co-decision" as for some measures outside the fiscal field.[21] Where a fiscal measure also has as its objective, the furtherance of the establishment of the internal market, it will also have to be based on Article 95 EC (formerly Article 100A), as was the case of the Customs Code referred to above.

The legislative consultation process organised by the EC Treaty is designed to obtain both democratic and also technical contributions. The democratic input comes from the Parliament, which is now elected by direct universal suffrage.[22] Moreover, nationals of Member States have citizenship of the EU[23] and, as such, have the right to vote and stand as a candidate in elections to the European Parliament in the Member State *in which they reside*, under the same conditions as nationals of that State.[24] The technical input to EC legislation comes from the Economic and Social Committee which consists of representatives of the various categories of economic and social activity, in particular, representatives of producers, farmers, carriers, workers, dealers, craftsmen, professional occupations and representatives of the

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19 Even in the case of multilateral conventions adopted pursuant to Article 249 EC, the Commission in practice has to take the initiative and make proposals to the Member States.

20 Article 250 EC (formerly Article 189A).

21 See, for example, Article 95 EC, formerly Article 100A, which requires the co-decision procedure under Article 251 EC, formerly Article 189B, for internal market measures; and also Article 71 EC, formerly Article 75, which, in matters of transport, requires the co-operation procedure under Article 252 EC, formerly Article 189C.

22 Article 190(1) EC, formerly Article 138(1).

23 Article 17(1) EC, formerly Article 8(1).

24 Article 19(2) EC, formerly Article 8B.

general public.[25] Originally the idea was that the Economic and Social Committee would be the vehicle for public consultation over proposed legislation, in much the same way as Government departments issue consultation papers before a parliamentary bill is drawn up in the UK. It soon became apparent that, by the time the Economic and Social Committee received a Commission proposal, it was very difficult to make substantial changes to the Commission's general approach. For this reason, industry and lobbyists have developed the practice of making informal contacts with Commission staff before a proposal is finalised, in order to provide essential technical input. For example, when the original Capital Adequacy Directive[26] was still in embryonic form within the Commission services, there were numerous informal contacts from the financial services industry in a behind the scenes debate as to whether to follow the German or the US approach to capital requirements for investment business risk. This example illustrates the importance of understanding the internal procedures within the Commission. The internal procedures within the other institutions are also important, from the lobbying point of view, and so this article will finish with a brief outline of these.

A proposal for EC legislation begins as an internal document within the Commission directorate responsible for the subject matter. In the case of taxation and customs, the directorate responsible is now DG Taxation. The Commission directorate may consult informally with industry and also with the Member State representatives. Once the proposal has been finalised as a draft, it is adopted formally by the Commissioners, as a college, and immediately forwarded to the EU Council, to the Parliament and to the Economic and Social Committee. Within the Parliament, there is first a debate on the general principle, and then the proposal is examined in committee. The *rapporteur* appointed in the committee has quite an influential role on the general direction and progress of the committee's examination. Ultimately the *rapporteur* draws up a report which usually recommends that the proposal be adopted subject to certain amendments. The report is then submitted to the plenary session for a vote. The resolution issuing from such vote and the committee report form the basis of the Parliament's opinion to the EU Council and to the Commission. In fiscal matters that do not involve internal market matters, the role of the Parliament ends there. If there is an internal market element to the Commission's proposal the Parliament will be given a second reading at a later stage, and will take part in the final adoption of the proposal. Since this procedure is not normal in fiscal matters, it will not be described here.[27]

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25 Article 257 EC (formerly Article 193).

26 Council Directive 936/EEC, OJ L141, 11th June 1993, p.1

27 The reader who is interested may consult any of the standard textbooks on EC law, notably Wyatt & Dashwood, European Community Law, Third Edition, pages 41 to 43.

The procedure within the Economic and Social Committee is similar to that within the Parliament, and the resulting opinion is also forwarded to the EU Council and to the Commission. The Commission may, if thought fit, amend its proposal in the light of the opinions issued by the Parliament and the Economic and Social Committee. It may also amend the proposal for its own reasons, although if any such amendment involves a substantial change from the texts provided to the Parliament and the Economic and Social Committee, it will be necessary to consult these bodies over the new text.

Once the Council has received the opinions of the Parliament and the Economic and Social Committee, the matter is examined by the Committee of Permanent Representatives (COREPER). If the Member State representatives agree to the proposal, the matter is placed on the so-called "A List" for adoption without debate. If the Member State representatives do not agree with the proposal as forwarded, they first try to resolve their difficulties in committee. If no agreement can be reached in this way, the matter must be sent to the Member States' Ministers for debate in Council, and ultimately for a vote. Since, in all fiscal matters outside the customs area, unanimity is required, any one Member State, in effect, has a veto. This is why the failure rate for proposals in the fiscal area, excluding customs, is relatively high.[28] The Ministers in Council can ask the Commission to amend a proposal in order to make it more palatable. This the Commission can do, subject to the reservation made above about having to re-consult the Parliament and the Economic and Social Committee on substantial amendments. The Council may also amend the proposal itself by unanimous decision, and then adopt the proposal as thus amended (again by unanimity in fiscal matters other than customs). It can be seen that, in fiscal matters other than customs, all the power centres in the Council, where the Member States have retained the sovereignty to adopt EC legislation, and individual Member States have retained a sovereign power of veto. Traditionally, the justification for this was the claim that, since economic policy was not harmonised by the EC Treaty, Member States had to retain sovereign power over national fiscal policy, because this was one of the principal levers of economic intervention. That argument has lost some of its force within the Member States included in the euro-zone because they are subject to the common discipline of economic and monetary union in accordance with the provisions of the EC Treaty and under the supervision of the European Central Bank. Nevertheless, the Treaty of Nice leaves unchanged the prerogative of the Member States in the fiscal area. Thus, one could conclude tentatively that the creation of EC tax law through legislation will continue to be hampered by national interests. For this reason, the

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28 For example, failure of the proposals on the carry-over of losses, on the taking into account of losses and of permanent establishments and subsidiaries situated in other Member States.

role of the Court of Justice will be of paramount importance in ensuring that national fiscal measures do not obstruct the functioning of the internal market.