The Prospects for European Income Tax Rules

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1. Background
The European Union (hereinafter EU or Union) is a single common market of 28 Member States (hereinafter Members). To achieve the objectives of single market, the EU has adopted a single customs tariff for the region and intervened to closely control national VAT systems. To date, it has not displayed willingness to take similar action with regard to Members’ income tax systems. This paper argues this situation may not persist over time, putting forward three reasons the EU may shift its policy of limited intervention to one of the comprehensive intervention, not unlikely the approach it has taken in the field of VAT.

As there is no supranational (‘federal’) direct taxation 1 at the level of European Union, the EU direct tax law is essentially aimed at the establishment and functioning of internal market. 2 The governing treaties – the ‘constitutional’ document – 3 proclaim direct taxes generally as a realm of Members 4

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1 While there might be other forms of direct taxes prevalent in the national jurisdictions of Member States of the European Union, this article refers direct taxation to income taxation i.e., personal and corporate taxes.

2 On ‘constitutionalization’ of internal market, see, for example, Article 3 of the Treaty on European Union (Art. 3 TEU) and Article 26 of the Treaty on the Functioning of the European Union (Art. 26 TFEU). References to single, common or Union market in this paper will effectively mean internal market. From policy perspective on how the notion of internal market occupies core of the EU agenda, see, e.g., Mario Monti, A New Strategy for the Single Market at the Service of Europe’s Economy and Society, a report to the President of the EU Commission J. M. Brosso (9 May 2010).

3 The treaty creating the European Economic Community (EEC) in 1957 or the Treaty of Rome, (and the subsequent treaties amending or replacing earlier documents such as Single European Act (SEA) 1986, Maastricht Treaty 1992, Treaty of Amsterdam 1997, Treaty of Nice 2001, Treaty of Athens 2003, and) to date the Treaty of Lisbon 2007 (effective 1 December 2009) are generally named as governing treaties in this paper. They are also referred to as the European Community (EC) law (after Maastricht), or the EU law (after Lisbon), and set out the Union’s constitutional basis. For official text of Treaty of Lisbon, see consolidated versions of the treaty on European Union and the treaty on the functioning of the European Union, signed on 13 Dec. 2007 (O.J. 2010/C 83/01, 30 Mar. 2010). To refer to official text of one of its forerunners as amended till the Treaty of Athens 2003, see consolidated versions of the treaty on European Union and of the treaty establishing the European Community signed on 16 Apr. 2003 (O.J. 2006/C 321/ E/1, 29 Dec. 2006).

4 The term ‘constitution’ of the Union in the paper also refers to respective Treaties in force over time, and may be regarded as ‘quasi or de facto constitution’ as is the status of the EU which according to Patrizio Bianchi, “Subsidiarity and Its Significance”, in Pat Devine et. al. (eds) Competitiveness, Subsidiarity and Industrial Policy, pp. 42-78 (Routledge 1996), at 43 represents a polity that is less than a federation but much higher than an international organization; on similar views concerning status of the EU polity, see also Longo, infra note 20.

5 Areas of exclusive Union competences (Art. 3 TFEU) as well as areas of competences shared by both the Union and Members (Art. 4(2) TFEU) are specified under the EU law. None of these confers the competence over direct taxation expressly to the Union. Hence by virtue of principle of conferral of residual powers (Art. 4(1) TFEU), stating that the competences not conferred upon the Union to stay (subject to Art. 4(1) TFEU) in hands of Members, direct taxation generally remains exclusive competence of Member States. Several legal commentators are also of the view that generally the Members retain tax competence; see, e.g., Charles E.
insofar as they do not infringe the EU law, in particular guarantees of fundamental freedoms, and prohibition principles enshrined thereunder to institute single market. Therefore, the national governments constituting the Union market are empowered to formulate their respective domestic tax policies. The result is that functioning of single market undergoes a parallel exercise of as many as 28 sovereign taxing jurisdictions. While the governing treaties, in general, make no explicit reference to direct taxes, one rather direct but scanty nexus to income taxation remained part of the Community law—an advisory provision inviting the Members to enter into negotiation with each other to abolish double taxation. The sole provision has also been done away with under the existing Union law since the Treaty of Lisbon came into force as of 1 December 2009. Subject to specified principles, the supranational powers to enact legislation (Directives) to govern the operation of national tax laws nevertheless had been—and remain—(inherent) part of the EU law.

Unlike VAT, which is subject to relatively strict central control by means of a VAT Directive that is based on explicit ‘constitutional’ provisions, the four legislative measures adopted in the field of income tax are significantly narrow in scope, dealing with particular and discreet issues. Supra-state legislation on income tax is constrained by two factors: First, the ‘constitutional’ framework, in stark contrast with customs tariffs, contains no expressed measure directing the EU to intervene in the income tax field. Hence the Members generally retain autonomy in this policy sector. The second is the fact that EU tax legislation requires unanimous consensus of all Members, a task

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5 Freedoms guaranteed (hereinafter fundamental freedoms) in the internal market under the governing treaties that may have nexus to direct taxation include freedom of movement to work (Art. 45 TFEU), freedom to right of establishment (Art. 49 TFEU), freedom to provide services (Art. 56 TFEU), and freedom of movement of capital and payments (Art. 63 TFEU).

6 Prohibitions declared in the internal market under the governing treaties (together with fundamental freedoms, hereinafter ‘freedom clauses’) that may also have nexus to direct taxation include prohibition on discrimination on the basis of nationality (Art. 18 TFEU), and prohibition on state aid (Art. 107 TFEU).

7 See second indent Art. 293 TEC.

8 To intervening national policies on direct taxes, the suprastate powers are exercised and governed by schematic legal order set out in the EU law, in particular provisions laying down areas of competence, and principles of subsidiarity and proportionality. For more details, see infra Sections 3, 4.

9 Directive is one of the forms of legislative acts. On other forms, see infra note 29. The existing legislation on direct taxes (see infra part 2.3) is enacted exclusively in the form of Directives. Under the EU law, Directives are binding in nature but do not have the direct effect. The doctrine of direct effect, based on the European Court of Justice’s ruling in Case C-26/62 Van Gend & Loos, stipulates that certain provisions (or instruments) of the EU law inherit legal force that by virtue of direct effect are effective in Member States without being enacted into domestic laws. For more details on principles of direct and indirect effect, see, e.g., Karen Davies, Understanding European Union Law (5th ed. LLB Ebooks Corporation 2013), at 75-79 (accessed 7 Aug. 2013). On evolution and development of the principle of direct effect, see also, Bruno de Witte, “Direct Effect, Primacy, and the Nature of Legal Order”, in Paul Craig and Grainne de Burca (eds) The Evolution of EU Law, pp. 323-362, (2nd ed. Oxford University Press 2011).


11 See infra part 3.2.2

12 See infra part 2.3; each Directive is fairly limited in scope and deals with specified issue.

13 See supra note 4.

14 For direct taxation, existing legislative instruments (Directives) are based on Art. 115 TFEU which requires unanimity of Members (each represented by respective minister in the Council of the EU). The unanimity
difficult to achieve. With no change in the unanimity requirement to adopt direct tax legislation, no dramatic shift could be foreseeable in the near future. Nevertheless, as to whether the dynamics of ‘balance of powers’ in the post-Lisbon period hints at entering a new evolutionary phase of an ‘ever closer Union’ 15 – insofar as changing dynamics for the prospective income tax initiatives are concerned – might need closer examination. Of the two key restrictions posed to the supranational income tax legislations, this paper thus examines the first constraint to the Union-wide actions in terms of powers on direct taxation generally vested in the Members.

Investigating a legal regime within the EU law, however, is a challenging job from various perspectives. First, it engages examination of a (quasi) constitutional frame of a unique set of law spotted exceptionally by legal scholars ‘as a blend of international law, national constitutional law, and federalism’.16 Second, such an exercise becomes a rather uphill task if the analysis involves a legislative regime like the one for direct taxes that does not exist in expressed terms. Defining four corners of Union action in this area within the division and exercise of power framework 17 could hardly be visualized without immense legal complexities. This study argues lawmaking, in the multilevel governance structure, as an ever evolving multidimensional competence, and attempts to explore prospects for EU-wide legislative initiatives on direct taxation in the post-2009 milieu since the latest legal order came into force. In addition to new legal schema, calls to probe plausible future developments on tax rules are also backed by the growing needs to increase competitiveness of businesses and to protect erosion of revenue bases in an already crisis-stricken jurisdiction.

In the remaining part of the paper, Section 2 provides an insight into the character of implied sources to exercise powers on direct taxes in the EU law, and makes a concise appraisal of its existing legislation. Section 3 analyses factors embedded in the EU legal system that could impact Union actions in this policy sector. Section 4 tracks the historical course on how the supranational competences evolved and attained constitutional strength. It also reviews in-depth the developments of legislative framework concerning direct taxation originating from the undergrowth of single market imperatives over time. Section 5, in seeking response to why to have an EU-wide income tax policy, explores the post-Lisbon legal developments having prospective proposition for supranational competence in this area. It also examines the rising economic compulsions to invoke legislative apparatus for making supranational tax rules in the jurisdiction. Finally, it evaluates

criteria on tax legislation has been named by many commentators as ‘veto power’; see, e.g., Michael J. Graetz and Alving C. Warren, “Income Tax Discrimination and the Political and Economic Integration of Europe”, Yale Law Journal, vol. 115(6), pp. 1186-1255 (2006), at 1190-1191.

15 A commitment of Members “[t]o create an ever closer Union......in accordance with the principles of subsidiarity” was inserted in the preamble of the Maastricht Treaty, and continues to exist there in the Treaty of Lisbon.


17 See, e.g., TEU and TFEU, supra note 4. On constitutional plan of ‘division of powers’ between the EU and Members, see Art. 4 and 5(1) TEU (principle of conferral of competences), Art. 2 TFEU (general scope of exercising competences), Art. 3 TFEU (EU exclusive competences), Art. 4 TFEU (EU shared competences), Art. 5 TFEU (ensuring coordination), Art. 6 TFEU (EU support, coordination actions), Protocol No. 25 (on exercise of shared competences), Declaration No. 18 to the Treaty of Lisbon (principles of de-conferral of shared competence), etc. On constitutional plan to ‘govern the use of non exclusive competences’, see Art. 5 TEU and infra part 3.3.
growing needs to rely on the legislative functions, and not the judicial rulings, in EU tax policy making. Section 6 draws a conclusion.

2. Sources and exercise of EU powers to legislate income taxation
The EU law, in explicit terms, is silent on legislative powers relating to income tax policy as the realm has been generally left to the Members. The supranational power to legislation is therefore derived indirectly from two major sources. One is the notion to create a single market in accordance with the fundamental freedoms and non-discrimination principles enshrined in the EU law. If national tax policies do not adhere to these principles and tend to impair the functioning of single market, a Union intervention might be necessitated. Second is a general authority or legal basis to act in order to integrate those national rules (including income taxes) which are violative of the single market imperatives. The Section explains these two inherent sources to legislate besides a concise detail of existing legislative instruments adopted in this policy area.

2.1 The powers inherent to single market principles
Since the days of the treaty establishing the European Economic Community (hereinafter EEC Treaty or Treaty) in 1957, the EU law does not mention direct taxes in explicit terms. The one and only explicit but flimsy reference that existed – concerning Members to strive to eliminate double taxation – also does no longer exist since the Treaty of Lisbon came into force. Despite lack of any directions and absence of its explicit mention in the corpus of the primary law, income tax competence remained very much in existence, and still exists, as embedded in the ‘multilayered’ EU law. The single market principles i.e., the freedoms of movement to work and capital, providing of services and right to establish together with prohibition on state aid and non-discrimination on grounds of nationality (hereinafter freedom clauses) create room for an EU role in the field of direct taxation.

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18 See supra note 7.
19 Primary law, in the EU parlance, refers to governing treaties, whereas secondary law refers to legislation enacted thereunder such as Regulations, Directives, Decisions, etc.
20 The expression ‘multilayered’ in this paper highlights specific design of the EU law that encompasses a unique mix of national and international laws; see, e.g., Michael Longo, Constitutionalising Europe: processes and practices, (Ashgate 2006), at 11; the author, in the context of the European integration, observes that ‘The EU has been described as a multi-level governance; a postmodern polity; a confederation; a quasi-federal system featuring pre-federal institutions; a sui generis legal order...’ and so on. See also supra note 16 and accompanying text.
21 For constitutional authority on each of the ‘freedom clauses’, see supra notes 5 and 6. The underlying legal design of these clauses hint that economic agenda generally but consciously takes precedence over political. E.g., while guaranteeing freedoms (and prohibitions), the EU law specifies certain exceptions not covered under the guarantees, such as freedom to work in the public service (Art. 45(4) TFEU), right to establishment in exercise of official duty (Art. 51 TFEU), provide service in exercise of official duty (Art. 62 in conj. with Art. 51 TFEU). These exceptions to freedoms in the internal market exclusively relate to public sector activities, indicating that the political angle of integration seems to take rather back seat. Likewise, free movement of capital and payments meant to steering the investment agenda of the entrepreneurs is also primarily economic and non-governmental in nature. In the same vein, prohibition on state aid that has been termed incompatible with internal market to avoid distorted competition and provide level playing field to the undertakings also emphasizes more of an economic coherence than the political harmony of public sectors. Constitutional exceptions to state aid clause (Art. 107(2) TFEU) are exclusively those meant for non-profitable purposes. Amongst the freedom clauses, non-discrimination on nationality is the only clause where the economic angle might appear to be secondary to the social and political one.
As long as national jurisdictions comply with the freedom clauses in terms of having taxation rules reasonably compatible to those of the single market, hypothetically, there would arise but little need to legislate EU-wide income tax rules. In practice, however, it is conceivable that several situations triggered by parallel exercise of multiple sovereign tax policies might inevitably end up in derogation to the guarantees ensured under the freedom clauses. At these particular junctures in the past, considerations to have Union-wide tax measures kept surfacing from time to time. Owing largely to dual constraints posed to tax legislation pointed out in Section 1, such considerations have been enacted into laws on a very small scale while others either could not translate into binding acts or awaiting final word.22

For general conception, to trace implicit seamless story of direct tax law, three constitutional commitments put together could practically serve as threads (prerequisites) to ‘interweave’ broad contours of primary direct tax law of the Union. (1) Constitutional obligation to constitute single market 23 in accordance with freedoms and prohibitions enshrined under governing treaties.24 (2) An authorization or legal basis to act for removing potential disparities and to integrate national tax rules,25 and (3) while doing so, the Union action to remain within the four corners envisioned under the regulatory clauses.26 Within this premise, a potential EU action on direct taxation is profoundly bound to adhere to these constitutional contemplations. Of the three ingredients, the last one does not confer the competence, and is an overseeing provision as explored in part 3.3. The first two prerequisites are the sources of competence attribution that respectively inherit obligation and legal authority to act.

2.2 An implicit legal basis to remove disparities

The application of a specific ‘platform’ (legal basis) is extremely relevant to initiate a given piece of legislation. It serves as a legal tool to translate the intents (legislative agenda) into actions (enactments). Just as potential onus to intervene national income tax rules is inherent to single market imperatives, likewise, the legal foundation to take action is also implicit to a general legal basis. The basis set out in Article 115 TFEU authorizes the EU to integrate those national laws (including income taxation) that directly affect the establishment or functioning of the single market.

22 Some of the legislative initiatives pursuant to eliminating specified disparities and bringing approximation in direct taxes ended successfully in adoption of Directives (see infra part 2.3); while others are either pending (see, e.g., Commission’s proposal, infra note 174) or withdrawn (see, e.g., infra note 133).

23 See, for example, specific obligations assigned to the Union, in specific, under Art. 3(3) TEU: “The Union shall establish an internal market.”, and corresponding powers vested in the Union, in particular, under Art. 26 TFEU: “1. The Union shall adopt measures with the aim of establishing or ensuring the functioning of the internal market, in accordance with the relevant provisions of the Treaties. 2. The internal market shall comprise an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties.”

24 See supra notes 5 and 6. The ‘freedom clauses’ serve as prime vehicles to achieve the task of single market.

25 These provisions embody those tools which are destined to provide precise (legal) base, and work as ‘launching pad’ for the legislative acts. Consequently, to initiate legislative actions in different areas, there are several constitutional ‘platforms’ (bases); see, e.g., infra note 27.

26 A legislative action of the Union in the area of direct taxes while fulfilling its obligations to actualize internal market may tantamount to intervention into the domain generally a Members exclusive area. This makes (legal) equilibrium of the Members-Union competences convoluted. In any case, the equilibrium has to be in compliance with subsidiarity and proportionality rules (see infra part 3.3) that govern the legislative acts on all areas of EU non-exclusive competences including that on direct taxes.
In order to act to integrate Members policy areas including the one at issue, the authority crafted in this legal basis inherits multiple propositions: First, it is a constitutional prerequisite to initiate a legislative act. Second, it determines voting criteria – qualified majority or unanimity – to enact legislation that in turn has its own ramifications. Third, the legal basis in question, stipulates to adopt Directive as form of legislation amongst multiple forms (such as Regulation, Directive, Decision, etc.) specified in the EU law. Directive is a form of binding legislation but allows Members liberty to choose modalities to transpose it into national rules to achieve its objective. Thus the legal basis also has affinities with the state-suprastate ‘power-sharing formula’ envisioned under the EU legal system. This, however, may not end the full story of legal basis in the legislative processes. On case-to-case basis, the legal tools may also be indicative of the schema of other broader guidelines – relevant but scattered elsewhere – on exercise of powers in the ‘multilayered’ constitution.

27 “Legal acts shall state the reasons on which they are based …” (Para 2, Art. 296 TFEU). On various legal bases for legislative actions in different policy sectors, see, e.g., Art. 14, 16, 18, 19, 21, 22, 23, 24, 25, 33, 43, 46, 48, 50, 51, 52, 53, 56, 59, 64, 65, 75, 77, 78, 79, 81, 82, 83, 84, 85, 86, 87, 88, 89, 91, 95, 103, 109, 113, 114, 115, 116, 118, 352 TFEU, etc. A few legal bases are general in applicative character and may act for legislative measures in multiple sectors; e.g. Art. 352 TFEU (known as flexibility clause by virtue of its applicative features), and Art. 115 TFEU (applied as legal basis for income tax legislation).

28 Unanimity criterion has been termed as ‘veto power’ in the hands of Members on direct tax legislation; see, e.g., Graetz and Warren, supra note 14. It is also widely considered as one of the leading factors impeding legislation on direct taxes in the EU; see, e.g., Tracy A. Kaye, “Direct Taxation in the European Union: From Maastricht to Lisbon”, Fordham International Law Journal, vol. 35(5), pp. 1231-1259 (2012), at 1232.

29 Legislative acts in the form of Regulation, Directive, and Decision are binding, and those in the form of Recommendation and Opinion are non-binding. While both Regulation and Decision are binding in entirety, and therefore of direct effect, the former is generally applicable to all Members, unlike the latter which applies to whom it specifies. In comparison, a Directive is a type of legislation applicable to whom addressed but lacks the direct effect with the result that Members are free to choose form and modalities to integrate it into their national laws with an obligation to the effect that the results desired by it must be achieved (see Art. 288 TFEU; on principle of direct effect, see supra note 9). Generally, legal base envisages as to which form of legal act should be adopted. Perceptibly, enactments such as Regulations by virtue of their direct effect will be stronger in legal force and as well as effective towards achieving objectives than Directives, and so forth. In certain cases, there may not be expressive specification as to which form of legal act needs to be adopted; for instance, the VAT Directives refer Art. 113 TFEU as its legal basis though there is no mention of any precise legal form under these provisions. Under such circumstances, the EU law (Para 1, Art. 296 TFEU) calls for type of act to be adopted on case-to-case basis in accordance with principles of proportionality. Consequently, this characteristic of a legal base and proportionality rule factually go hand in hand (see infra note 107 and accompanying text).

30 For instance, direct tax legislations adopted as Council Directives 2010/24/EU of 16 Mar. 2010, and 2011/16/2011 of 15 Feb. 2011, respectively known as Directives on recovery of tax claims and administrative cooperation, in their preambles, place reliance on multiple legal bases as “having regard to the Treaty on the Functioning of European Union, and in particular Articles 113 and 115 thereof…” Insertion of an additional legal base (Art. 113 TFEU) is factually indicative of conferring competence in addition to what is required for direct taxes, and hence render both Directives equally applicable to the indirect taxes. Another incidence proposing departure from ordinary legal foundation (Art. 115 TFEU) was witnessed at the time of consideration of proposed CCCTB Directive by the EU Parliament. The Committee on Economic and Monetary Affairs of the Parliament sought legal opinion from the Parliament’s Committee on Legal Affairs on the Legal Basis regarding possible inclusion of Art. 136 TFEU as additional legal base, besides the usual Art. 115 TFEU, so as to extend necessary platform to the proposed Directive for making it effective in the Eurozone instead of the EU. Though the Committee on Legal Affairs declined the multi-base proposal in this particular instance for want of compatibility between the two legal provisions as recorded in its decision of 23 Jan. 2012, it does provide a fair insight on rationale adhered to the competence-specific employment of ‘platform’ compatible to discussion in question. Committee’s decision at http://www.europarl.europa.eu/sides/getDoc.do?pubRef=-//EP//TEXT+REPORT+A7-2012-0080+0+DOC+XML+V0//EN (accessed 24 Jul. 2013).
2.3 Exercise of implicit powers until now

Based on the implicit notions, the EU has exercised very limited legislative powers to date in the area of direct taxes. The adoptions of a few narrow and discreet measures predominantly focus on qualifying corporate taxpayers. The legislative instruments tend to limit double taxation by targeting tax consequences of specific cross border economic situations or transactions of specified taxpayers. In addition to assistance and recovery measures, four such instruments (Directives) until now have been issued by the legislator (the Council of EU) on the recommendations of the executive organ (the Commission). The adopted legislation generally aims at the elimination of specified double tax burdens likely to arise pursuant to divergent national tax policies in the internal market. A concise description on each Directive to follow evidences their much limited scope.

The Parent-Subsidiary Directive is meant to bring the interstate and intrastate companies at parity by removing tax disadvantages to the former. The legislation mitigates economic double taxation between parent – subsidiary by stipulating that state of parent should either exempt the dividend distribution or extend an indirect credit of tax payments by subsidiary. The Directive prohibits the state of subsidiary compulsorily from imposing withholding tax on the dividend to avoid juridical double taxation. The scope of the Directive is dividend-specific and limited to the related companies, and that too is pre-conditioned to qualifying minimum holding requirement.

The Merger Directive, at the time of merger, division, partial division or transfer of assets, prohibits the state of the transferring company to tax any built-in capital gain. The taxation of capital gain is not let off altogether, rather deferred. In case taxation of gain is not deferred, the transferring state would tax the difference between the book value and current value at the time of transfer, and the new state of residence would tax the difference between book value and sale value of assets. The deferral, to mitigate double taxation that might have happened pursuant to differences in timings of taxation, ensures that both Members tax at the same time when actual sale of assets takes place. The Directive also accommodates the possibility of transfers involving a third Member, providing that the state of transferring company either to forego its taxing right or while taxing the gain allow a credit for the taxes that the permanent establishment would have paid on these gains.

The Interest and Royalty Directive makes it obligatory on the state of paying company to refrain from charging withholding tax. The Directive also solves the problem of double taxation by prohibiting withholding tax in state of subsidiary as well as of permanent establishment. The issues relating to limitation of credit method ordinarily stemming from excessive tax deductions in source

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32 The Council of EU (represented by relevant minister of each Member) together with EU Parliament constitute legislature of the Union. The EU Commission is the executive organ of the jurisdiction and is entrusted with remarkable functions including proposals to the legislator on draft legislative acts.
34 Council Directive 90/434/EEC of 23 Jul. 1990 on common system of taxation applicable to mergers, divisions, transfers of assets and exchanges concerning companies of different Member States (ibid, at 1-5), as amended from time to time.
countries compared to actual tax liability in residence country are eliminated. The scope of the legislation is also limited similar to that of the Parent-Subsidiary Directive.

The Savings Directive\(^\text{36}\) extends to taxation of income derived from interest by individuals. Members in the capacity of source country, in general, do not impose withholding tax on interest income of individuals. Rather the information is passed on to the residence country for tax purposes. On transitional grounds, a few Members\(^\text{37}\) have been entitled to levy withholding tax on interest incomes, and the residence states are obliged to apply credit method to avoid double taxation. In case the tax liability works out less than tax withheld at source, the residence states have to refund the excessive amounts to individual taxpayers. The scope of the legislation is exclusively limited to income characterised by interest earnings.

3. Factors affecting legislative powers on direct taxation

Leaving the political (unanimity) aspect aside, we consider three constitutional factors here that could impact the EU powers to formulate income tax policy. The first is the primary source that delegates legislative competence to the Union action in terms of sub-textual character inherent to the single market clauses. The second is an authority vested in the non-tax-specific legal basis to intervene (national) tax laws impeding the common market. The third is a factor that otherwise does not confer the competence itself but impacts legislation by its regulatory feature. This aspect oversees the justification and reasoning of the intended action, and restricts undue intervention into national (tax) systems through a constitutional framework under the principles of subsidiarity and proportionality.

3.1 Powers of implicit nature

The fact that it is submerged below the other powers only may limit the legislative competence on direct taxes. The powers to legislate are derived indirectly from other constitutional obligation to institute internal market. The implicit character might have at least two major implications for the policy area under examination. First, an EU action in this area to certain extent has to enter into the territory of the doctrine of derived powers. The restrictive designs generally adhered to the doctrine in extending powers from the principal framework to the derivative are explicable.\(^\text{38}\)

Second and more evident, is the fact that the idea of internal market and related principles, on which the income taxation powers chiefly rely upon, are dynamic concepts that is ever evolving since the founding days. For instance, the fundamental freedoms, the core elements constituting common market, had yet to unfold in a transitional period (12-15 years) envisioned by the EEC system when founded.\(^\text{39}\) Unless the transitional episode, in theory, is over and objectives successfully achieved, the derived powers conditional to them (as income taxation) would have little meaning. With the

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\(^{37}\) These Members include Austria, Belgium and Luxembourg. As of 1 January 2010, however, Belgium has also switched over to the standard procedure laid down in the Directive.

\(^{38}\) See, \textit{e.g.}, Antonio Tizzano, “The Powers of Community” in Commission of the European Communities in A Tizzano (ed), \textit{Thirty Years of Community Law}, pp. 43-68 (Office of Official Publications 1981), at 47 et seq; the author refers to the complexities of application of the doctrine from judicial perspective.

\(^{39}\) See Art. 8 of treaty establishing EEC (Art. 8 EEC); the clause envisions 12 years transitional period, extendable to 15, for gradually establishing common market in accordance with the then scheme of areas.
specified period over, the standing of single market would get material meaning to the extent of realization of the initial tasks, and so do the corresponding powers originating from it. Likewise, whenever new spheres kept gradually adding or the existing ones expanding under various amendments, the status of single market might migrate accordingly over time. With the assigned objectives of integration are gradually accomplished in the added/expanded policy sectors, the market unification takes a new shape, and so does the scope of the implicit power derived from it.

Thus the changing dynamics of conferral of implicit power in the area of income taxation, the prime component of lawmaking, does not exist in a watertight textual milieu of EU law. Instead, it is a sort of active ‘legislative fiction’ – applicative characters of which are marked by the absence of visible semiotics in the EU law. This phenomenon of implied power becomes relatively comprehensible when traced as a common evolutionary thread passing along past to the present and then leading to the future as discussed in Section 4.2.

3.2 Non-specialised legal basis
As a vital tool of legislative apparatus, the application of a general legal basis is equipped with normative powers seemingly restraining extensive Union actions in this area. In what follows, seeks to compare and explicate how a non-specialist general legal basis applied to (implicit) income tax regime could substantially differ in outcome from an area-specific one such as that meant (explicitly) for VAT regime – a sister policy area.

3.2.1 Basis to integrate income taxation
With no expressed mention of direct taxes, how a legal basis empowering tax legislation could possibly be determined is part of the evolutionary tale on taxation powers (part 4.2.2). Here we argue that once the legal basis is established, how the mandate embedded in it may unfold the broad story of ‘dos and don’ts’ of direct tax legislation. The constitutional provision (Art. 115 TFEU) invoked so far as legal basis to legislate direct tax rules, placed in the segment (titled) ‘approximation of laws’, reads as [italics and emphasis added]:

‘[t]he Council shall acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and Economic and Social Committee, issue directives for the approximation of such laws, regulations or administrative provisions of the Member States as directly affect the establishment or functioning of internal market.’

A legal dissection of the text reveals that the word ‘unanimously’ in the text refers to the veto factor impeding the tax legislation as pointed out in the introductory part, and is beyond the scope of this study. At least three other expressions instrumental to determine relative authority to integrate direct taxation of Members nevertheless merit consideration: ‘directives’, ‘approximation’, and ‘directly affect’. For instance, of all the legal acts of binding nature, ‘directives’ might take precedence over other forms as they are not to be directly implemented but rather transposed in national statutes. Directives not only can intervene the national laws but simultaneously provide Members a ‘breathing space’, a befitting pursuit in an area (broadly) of their exclusive competence.

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40 On addition/expansion of areas of influence under some of the amendments, see infra part 4.1.
41 As actual legislative measures taken in the field of direct taxes were mostly adopted before TFEU came into force, therefore, legal basis of these instruments have equivalents of Art 115 TFEU i.e. Art. 94 TEC (in 2003), and Art. 100 EEC (in 1990).
A Regulation or an instrument of direct effect could better correspond to an area of extensive and explicit EU competence which obviously is not the case with direct taxes.

‘Approximation’ (relative to the term ‘harmonisation’ used for indirect taxes), likewise, might also carry connotations for a relatively softer penetration to interfere national laws. The words ‘directly affect’, in the same token, underpin a restraint on intrusion into national rules and subjects it to if – and only if – such rules ‘directly affect’ the internal market. This is unlike indirect tax laws and other national laws of non-fiscal nature. In both latter situations, legal bases empowered to initiate integrative measures, are not necessarily pre-conditioned as to whether the (national) laws in question ‘directly affect’ the internal market or otherwise.

To sum up, in exercising legislative powers of the Union, the in-built legal plan of (general) legal base is not sufficiently self-contained to impart force to the actions at its own. It has empathy to house multiple traits for various policy sectors but it could be manifested only when the areas are spoken of in the EU law, which obviously is not the case with income taxation. No doubt, the implicit nature of legal basis may also not be beyond the traditional dynamism yet an action under implicit legal basis relying, in turn, on implicit powers might seemingly add to the convolution of potential actions.

How a general legal basis for income tax legislation inherits a different scope for Union action relative to an explicit and specialised one, such as that for value added tax (VAT), is illustrated below.

### 3.2.2 In comparison to VAT law

Unlike direct taxes, right from the EEC Treaty, indirect taxes have been expressly dedicated a distinct section in the law, titled ‘Tax provisions’, having (then) a precise legal basis i.e., ‘The Commission shall consider in what way the laws of the various Member States concerning turn over taxes, excise duties and other indirect taxes...can be harmonised in the interests of the common market. The Commission shall submit proposals to the Council, which should decide by unanimous vote....’. Separate chapters titled ‘Tax provisions’ were also devoted to indirect taxes under the subsequent Community laws and it so remains under the current Union law. With this concise preface on constitutional agenda for indirect taxes, the corresponding flow of the changing power dynamics for Union-wide VAT legislation may not be far from perception. The existing clause (Art. 113 TFEU) meant to serve as a legal basis to adopt VAT rules, read as [italics and emphasis added]:

> 'The Council shall acting unanimously in accordance with a special legislative procedure and after consulting the European Parliament and Economic and Social Committee, adopt provisions for the

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42 From the days of treaty establishing EEC to date, the words ‘harmonisation’ and ‘approximation’ have been employed in the legal basis meant respectively for integration of indirect taxes and direct taxes (embedded in general legal basis). On further legal discern between the two terms in context of EU law, see infra note 51.

43 For indirect taxes, see infra part 3.2.2; for other laws of non-fiscal nature, see Art. 114 TFEU (equivalent to Art. 95 TEC under Treaty of Amsterdam, and Art. 100a TEC under Maastricht Treaty).

44 Art. 95-99 EEC.

45 Art. 99 EEC.

46 Art. 95-99 TEC (under the Maastricht Treaty), and Art. 90-93 TEC (under the Treaty of Amsterdam).

47 Art. 110-113 TFEU.

48 Art. 113 TFEU replaced earlier Art. 93 TEC; the latter in turn was preceded by Art. 99 EEC. Substantially they are almost the same with gradual increase in degree of authority to harmonisation (in practice) from Treaty of Rome to the Treaty of Lisbon. The legal basis of main legislative measure taken for VAT (Council Directive 77/388/EEC supra note 10) refers both to Art. 99, 100 EEC as dual legal bases. The instrument was replaced by the existing VAT law (Council Directive 2006/112/EC supra note 10) with Art. 93 TEC as its single legal base.
harmonisation of legislation concerning turn over taxes, excise duties and other forms of indirect taxation to the extent that such harmonisation is necessary to ensure the establishment and functioning of internal market and to avoid distortion of competition."

Unanimous voting by the legislature, similar to that in case of direct taxation, is also obligatory to adopt legislative acts for indirect taxes. Why unanimity hinders much less while passing VAT law than it does for direct taxation, is not the subject of issue at hand. However, it can fairly be attributable, in varying degree each, to the political willingness of the Members and competence dynamics manifested by the constitutional terms right from the days of the EEC Treaty.49

For comparative analysis of legal bases of the two forms of taxation however, at least four expressions emphasized in the text are worth attention: First, contrary to direct taxes, the legislative instrument has not been restricted to Directives. The word ‘provisions’ 50 gives the legislature a liberty to adopt legislation beyond Directive to other forms such as Regulation or Decision subject to principle of proportionality (part 3.3). Second, the legal base contemplates ‘harmonisation’ of indirect taxes instead of approximation. The former seems to signify relatively deeper penetration into national laws (enhanced integration) when viewed in the context of constitutional scheme.51

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49 See, e.g., supra notes 44-47 and the accompanying text.
50 By virtue of the expression ‘provisions’ used in the legal foundation, Art. 296 TFEU (see supra note 29) becomes applicable to it. Thus the scope of choice to use legal tools, unlike direct taxes, can no longer be restricted merely to Directives. Based on the content and depth required at the Union level (proportionality), an action can also be enforced in the form of a Regulation or Decision to intervene national VAT regimes. Notwithstanding that the current instrument of VAT law in the Union is Directive, scope of its application and achieving integration is unrivalled to similar tool(s) adopted for direct taxation (see, Council Directive 2006/112/EC supra note 10; for brief discussion so far as relatively enhanced scope of EU actions in VAT is concerned, see also infra notes 53, 54; for direct tax Directives, see supra part 2.3). At the same time, irrespective of the fact that current instrument of Union VAT law is in the form of Directive, the authority conferred upon the legal basis for VAT to select and adopt other forms of legislative tools remains equally intact.
51 According to McLure supra note 4, at 379-380, ‘the term harmonization means different in the EU and the US (coordination is the more common word used in the US)’. Referring to Linda Senden, Soft Law in European Community Law (2004), at 45-46, McLure identifies three related concepts used in the EU discussions of tax policy: harmonization, approximation, and unification, and says that ‘harmonisation – and thus by implication approximation – refers to integration processes that do not lead to the creation of uniform law, but rather to the creation of common frameworks or legal rules establishing a common goal, which leave room for divergent national specifications’. Analysis in the study in hand, however, slightly differs from this interpretation, and develops a relative distinction between approximation and harmonization on the grounds set out in the peculiarity of two legal bases (Art. 99 and 100 EEC) under the EEC Treaty. Whereas Art. 99 EEC was applicable exclusively to the turn over taxes, excise duties and other indirect taxes, Art. 100 EEC was not intended to be direct tax-specific. By scope, the latter, as a general legal base, was extendable to all laws and regulations (and hence all powers) of the Members directly affecting common market. Both expressions essentially involve integration (and thus intervention) in the national laws (powers). The use of one expression covered a single, and that too, explicit area (indirect taxes), while the second expression covered several implicit (as well as explicit) areas. In these connotations, approximation relative to harmonisation is plausibly suggestive of a degree of ‘reluctance’ in accessing the national laws. The authors of the EEC Treaty appeared to be mindful of the Members uncertainty concerns over potential Community (now Union) actions in a range of unforeseen areas, ending up in two distinguishable words. A relative difference in two also gains evidence from the ‘harmonization’ achieved through sweeping VAT Directive of 1977 that hardly finds proportionately parallel actions in other areas through ‘approximation’ right during the first two decades of the Treaty. It is also noticeable that another legal base added to the EEC Treaty through amendment under the SEA 1987 (Art. 100a EEC) contains both expressions in it. Insofar as areas covered by this new legal base is concerned, coincidentally or otherwise, its design is more specific (covers less number of policy areas) than one under Art.
Third, it intensifies integrative scope by assigning ‘harmonisation’ (over and above internal market as general to) an additional but explicit objective to ‘avoid distortion of competition’. Likewise, for contemplating harmonisation initiatives, there is inter alia no legal obligation to pre-establish that the (national) laws in question ‘affect’ the internal market ‘directly’ (as under Art. 115 TFEU) or otherwise.

All these features, in aggregate, contribute towards powers to permeate deeper into national VAT regimes for their EU-wide harmonization. As a result, contrary to direct taxation, the specialized and explicit legal basis for indirect tax laws together with the flow from the expansive power dynamics concludes in (considerably) enhanced scope for Union-wide VAT policy making. The scale of the VAT legislation to date also evidences this. The Commission’s ongoing and prospective VAT agenda is

100 EEC but is certainly general (higher number of areas) compared to monistic specific legal base under Art. 99 EEC.

The distinction, however, may get fuzzy if the general legal base (Art. 100 EEC) is applied to (say) VAT area when, owing to cumulative effect of all VAT related legal provisions, the same base may also encapsulate the ‘harmonizing’ impacts in it (for hypothetical application of Art. 100 EEC to VAT, see infra part 4.2.2). Thus one may fairly suggest that harmonization, under the EU law, is a notion with integrative implications generally deeper than approximation. It may also be observed that the earlier VAT Directives (such as those adopted in 1967, 1977) had dual legal basis (i.e. both Art. 99, 100 EEC). This indicated at least two aspects of lawmaker: First, the lawmaker’s intents to assign inclusiveness to the act so as not to skip any legal authorisation and secondly, relatively less clarity of demarcation between the two bases existing at the initial times as the general legal basis had yet not yielded any substantive act in direct tax area. In fact at the time of recast of VAT Directive in more recent times (2006), after the two legal bases have attained a sufficient level of clarity, only single but relevant legal basis (Art. 93 TEC, equivalent to Art. 99 EEC) has been relied upon. Some of the existing Directives (see supra note 31) still have dual legal bases (Art. 113, 115 TFEU) but their evident purpose is to extend the application of such procedural Directives both to the direct as well as indirect taxes.

The observation that ‘the term harmonisation means different in EU and the US’ (McLure, ibid), seems quite justified if viewed in the context that in the US, unlike the EU, harmonization and approximation are taken as one and the same. For instance, the US version in English translates the title of section 3 of the EEC Treaty as ‘Harmonisation of Laws’ (see, e.g., Treaty Establishing the European Economic Community, The American Journal of International Law, vol. 51, no. 4, pp. 865-954 (Oct., 1957), at 900); whereas the European English version translates the same title of the EEC Treaty differently as ‘Approximation of Laws’ (see, e.g., ec.europa.eu/.../documents/treaty/rometreaty2.pdf (page 34, accessed 24 May 2013)). Nevertheless, the use of the word harmonisation in a general sense to represent allied concepts may also not be misleading unless the EU legal context otherwise so requires.

52 The additional objective codified in the legal foundation proportionally delegates enhanced scope under the ‘balancing clauses’ to harmonize national VAT laws. To ‘avoid distortion of competition’, (in addition to standard broad objective of single market set out therein), the base also takes into account constitutional provisions laid down in chapter (titled) ‘rules on competition’ (Art. 101-109 TFEU), etc. This entrusts additional sanction to this base which in collaboration with other legal strengths translate into tremendously expansive legislative acts.

further suggestive of the same. For instance, based on studies and consultations, a draft legislation to adopt a common VAT return along the single market has been proposed recently in October 2013.55

3.3 Subsidiarity and proportionality

3.3.1 In general
The subsidiarity rule, a constitutional provision superimposed on the balance of powers, governs the exercise of legislative actions in all areas of non-exclusive EU competences. Since its introduction in the Community law under the Maastricht Treaty, the provision has been a subject of enormous academic discourse with a plethora of literature available on it. The distinctive provision when added to the (then) Community law read as [italics added]:

‘In areas which do not fall within its exclusive competence, the Community shall take action, in accordance with the principle of subsidiarity, only if and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member States and can therefore, by reason of the scale or effects of the proposed action, be better achieved by the Community.

Any action by the Community shall not go beyond what is necessary to achieve the objectives of this Treaty.’

Later, a protocol, and a declaration were also added to explain the procedure on application of subsidiarity. The provision in substance together with (an amended) protocol on application of these principles remains part of the Treaty of Lisbon. As an exceptional constitutional tool, it governs the exercise of Community powers in areas of non-exclusive competence. The scope of the principle does not extend to the conferral of competences, but rather it features a regulatory

58 For protocol and declaration on subsidiarity added through the Treaty of Amsterdam, see O.J. C 340/105-107, 140, 10 Nov. 1997.
59 Art. 5(3) TEU (subsidiarity and proportionality), Protocol No. 2 (on the application of these principles) annexed to the Treaty of Lisbon.
function. It may expand or confine actions while exercising shared-powers that have been entrusted elsewhere in the law. Every legislative act in related areas including taxation therefore, must undergo the test set forth by this principle. The evident criteria for the Union action of ‘passing’ the test are: No supranational legislative action shall be taken unless (1) the Members action cannot sufficiently realize the objectives, (2) the Union can perform better in doing the same (3) by reason of scale or effects of the action, and (4) any intervention by the EU should strictly not exceed the limit of attaining objectives (proportionality).

3.3.2 In taxation

Of various dimensions, the subsidiarity yardstick in tax policy area may largely be applicable at the interface of law and economics rather than law and politics. The Amsterdam addition on how to apply subsidiarity pronounces it as ‘a dynamic concept’ applicable to the process of lawmaking to achieve objectives of the TEC. The principle encapsulates diverse notions: while its efficiency and cost-benefit (economic) dimensions apparently flow from the provision itself, it has been termed as ‘first and foremost a political principle’. Besides, subsidiarity is also denoted as ‘a state of mind’ (political) and ‘a sort of rule of reason’ (legal, political, economic). Paucity of the case law on subsidiarity is another remarkable focus as the provision has yet not undergone extensive judicial review. As a multifaceted concept, academically it is ‘one of the most debated, analysed, criticized, despised and, in few cases, loved concepts of EU law’. The several aspects of the subsidiarity including its comprehensive discourse in relation to taxation are beyond the scope of this paper. The instant study would however concisely attempt to seek its regulatory interplay with the legislative competence on direct taxes.

The argument that the subsidiarity rule takes lego-economic dimension to oversee the Union actions in taxation takes backing from the birth place of this rule within the EU law. When environment was being added to the actionable spheres of the Community under the Single European Act (SEA), the subsidiarity (without being named) was embodied in the (then) Community law for the first time, and was applicable exclusively to the Community actions on environment. As within the newly assigned competence (on environment), it was possible that certain Community actions could encroach upon some Members without their consent by virtue of majoritarian voting, subsidiarity

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60 ‘This principle does not convey whether or not the EU has the power to act with regard to a specific policy’; Portuguese, supra note 57, at 233; the Commission’s report to the European Council on the adaptation of Community legislation to the subsidiarity principle COM (93) 545 final, 24 Sep. 1993, at 1 also explains that ‘Its function is not to distribute powers...The aim of the subsidiarity is, rather, to regulate the exercise of powers and justify their use’.

61 Para 3 of protocol, supra note 58; the provision also states that ‘It allows Community action within the limits of its powers to be expanded where circumstances so require, and conversely, to be restricted or discontinued where it is no longer justified.’

62 Commission, supra note 60.

63 Commission, supra note 60, at 2.

64 Commission, supra note 60.

65 Since the subsidiarity put in place in the TEC, in almost twenty years, there had hardly ten substantial cases challenging the provision before the ECI; Craig, supra note 57, at 80.

66 See Biondi, supra note 53, at 213.

67 See Art. 130r, 130s EEC added through the SEA; O.J. No L 169/01-29, 29 Jun. 1987.

68 See Art. 130r(5) EEC added through the SEA; ibid.

69 Some of the Community actions on environment could be contemplated by qualified majority voting; see sub-para 2, Art. 130s EEC, added under the SEA, ibid. This could leave the room for an act that some (opposing minority) Members might be concerned of. The subsidiarity insertion, to an extent, could potentially address it.
check therefore could mitigate their concerns to an extent. The introduction of subsidiarity calculus extendable to all non-exclusive powers under the Maastricht Treaty could also be a manifestation of similar concerns of Members pursuant to ‘voting ease’ extended to various policy sectors in those times.\(^{70}\) If the subsidiarity check is there to cater for sovereignty fears raised by the ‘voting ease’, political dimensions of the rule are explicable.

In the realm of taxation nevertheless the requirement of unanimous voting remained intact. Hence the lego-political role of the provision is bound to fade for taxation as the Members already have power to veto any initiative they deem as ‘unwarranted intrusion’. Taken strictly in political terms, the subsidiarity might thus appear to be a rather superfluous notion for taxation. This is where the lego-economic character of this dynamic principle triggers, and the economic parameters may take precedence over the political one when it comes to taxation. Subsidiarity criteria would thus take into account economic arguments of efficiency and cost benefit analysis to measure actions such as those meant to reduce cross-country spillover effects of tax policy or tax-induced distortions in the internal market.\(^{71}\)

4. Evolution of the implicit competence to legislation in income tax field

Nothing in the legislative regimes of the EU constitution makes sense as clearer as in the light of evolutionary developments of power equilibrium. This is due to the fact that the way supranational governance has evolved in the jurisdiction, seeking answer to the question, ‘who governs?’ changes over time.\(^{72}\) For income taxation, it was argued in the previous Section that the powers implicit to single market principles are fluid and dynamic. In fact, all the three factors considered to having a say in legislation are, \textit{stricto senso}, not compartmentalized. Considering each in isolation for their potential impacts on legislative outcomes might convey some broad outlines but not the fuller picture of their interaction in the legislative tale.

Hence, to frame the right perspective, the growth and allocation of powers in general, and the interplay of factors affecting legislative framework for income taxation in particular could be better traced along an evolutionary path. In addition, the peculiar and atypical role of the three main actors – the Commission, the European Court of Justice, and the Council – might also be hardly comprehensible in the legislative processes except in the light of past institutional interactions. Thus to facilitate such an analysis, what follows takes an excursion of contextual developments behind the changing balance of powers in the European legal system in general as seen in part 4.1, and then, in-depth, to their corresponding impacts on powers dynamics in direct taxes in part 4.2.

4.1 Allocation of powers in general

Much of the conferral of powers as developed in the EU law over time was not expressly embodied in the founding days. Historically, the treaty establishing EEC entered into force to institute an international economic organisation. Parallel to an international polity governed under international

\(^{70}\) See \textit{infra} note 83 and accompanying text.


\(^{72}\) Alec Stone Sweet and Wayne Sandholtz, “European integration and supranational governance”, \textit{Journal of European Public Policy}, vol. 4, issue 3, pp. 297-317 (1997), at 299; the authors, in the context of Community’s sites of policy making and competences to govern, observe that ‘Within the same policy sector, the answer to the question, ‘who governs?’ has changed over time.’
law where powers, save in explicit terms, are vested in the nation states, the surrender of national autonomy in the Treaty is also not conspicuous (in text) compared to what followed (in practice) at the subsequent phases. With the ‘division of powers’ not codified, the EEC system adopted the so-called ‘functionalistic approach’, and to achieve the entrusted policy objectives, legislation could be enacted by using appropriate legal bases scattered across the Treaty.

Despite the fact that the Treaty largely remained textually unaltered till 1987 when the SEA amended it, the status of ‘balance of powers’ in practice did not remain static. In evolutionary terms, the ‘mobility of competences’ was notably traceable during the 1960s and 70s which was indicative of expansions in the applicable dimensions of supranational powers: First, the exercise of commands between the ‘intergovernmental institutions’ (the Council and the Commission) gradually changed in the form of ‘comitology that developed in the undergrowth of the Treaty of Rome’. Second and more significant were those developments which led to the creation of a kind of power equilibrium that favoured the Community in a manner customarily designed for ‘federal’ structures. For instance, the European Court of Justice (ECJ or the Court) delivered certain rulings around the mid-1960s which led to ‘discovery’ of constitutional ‘traces’ in the Treaty. The Court held that the suprastate powers integrally vested in the Community law carried much deeper legal implications for national jurisdictions than what one would ordinarily consider to flow from similar plain text of an international convention. The consequent robust growth instituted supremacy (in EU parlance: primacy) of the Community law and created rights for individuals enforceable through national courts. Similarly, progress in expansion of Community powers beyond the textual illustration of the Treaty was also achieved, in part, by wider and frequent use of appropriate ‘enabling’ legal bases. Unlike the general authority attributed to typical international conventions, the outcome of supranational legal assertions together with actions inherent to legal bases (to legislate) laid broad foundations of the ‘constitutionalisation’ of the Union (then Communities) powers.

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74 Rossi points out that the division of powers between Members and the Community is not subject to text-based inertia but ‘mobile’ by nature; ibid, at 87 (cross-citation Tizzano, supra note 38, pp. 43-68).
76 After the Lisbon Treaty came into force, the Court was re-named as the Court of Justice of the EU (CJEU), however, this article would cite it as the ECJ as does most of the literature because at this point of time, historically, most judgments have been delivered and cited with the ECJ nomenclature.
77 E.g. The land mark decisions of the Court declaring certain provisions of the EEC Treaty to have direct effect and thus creating individual rights enforceable through national courts (ECJ Case C-26/62 Van Gend & Loos), and the verdict assigning the Community law primacy over national laws (ECJ Case C-6/64 Costa v. ENEL), etc.
78 Tizzano, supra note 38, at 46.
79 The Community was authorized to frame Regulations, Directives, and take Decisions (Art. 189 EEC) provided that these actions were supported by reasons (Art. 190 EEC) to achieve specified policy objectives in accordance with supra note 73 and accompanying text.
80 With reference to judicial developments on the ‘constitutionalisation’ of the Community law, see, e.g., J.H.H. Weiller, “The Transformation of Europe”, Yale Law Journal, vol. 100(8), pp. 2403-2484 (1991), at 2413-2419; the author states the ‘constitutionalisation’ as an ongoing process and suggests that since all major doctrines were in place by early 1970s, what followed were the refinements of these doctrines.
With this ‘competence baggage’, the Community law entered into a new phase of developments when the SEA (in 1987) codified significant amendments to the EEC Treaty that further strengthened the legislative authority of the Community.\(^{82}\) Despite lack of explicit classification to delimit competences between Members and the Community yet largely unaltered, the amendments led to remarkable shift by setting up a ‘legislative convenience’ to adopt Community-wide actions. This was achieved by replacing the condition of ‘unanimous’ voting with that of the ‘qualified majority’ in several legal foundations meant for exercising powers to realize policy goals.\(^{83}\) In addition, various other provisions were added to the Treaty to make the Community powers expressive and also extendable to certain new areas.\(^{84}\) These changes implied a relatively enhanced scope for the Community to act in the given areas. Nevertheless, certain legal bases were still left out of the ambit of ‘voting ease’ as they still needed unanimity for legislation.\(^{85}\) The distinction of unanimity and qualified majority voting patterns embodied in different legal bases could also be regarded as an indexation to determine extent of the Community powers in different areas. The amendments under the SEA therefore seemingly crafted a sketchy roadmap to prospective ‘power separation’. In this backdrop of limited but conscious application of diverging voting conditions, the general premise that ‘the division of competences between Member States and the European Community seems to have been gradually shaped not by a predetermined project, but according to specific needs’ \(^{86}\) holds rather more relevance to the pre-SEA era of the Community than to the subsequent periods.

The treaty establishing European Community (TEC, under the Maastricht Treaty) in 1992 \(^{87}\) was a cornerstone in advancing the agenda to exercise authorities set out under the SEA. Still marked by the absence of explicitly categorised competence, the TEC however further clarified and issued a revised list of Community tasks.\(^{88}\) The newly updated list now contained twenty or so activities where the Community could intervene.\(^{89}\) Thus on the journey from ‘internationalisation to federalisation’, a range of policy areas kept adding to the ‘job description’ of the Community. Centralisation of certain powers such as those for the establishment of customs union and removal of tariffs between Members set out in categorical terms right from the early days of the Treaty could

\(^{82}\) For detailed textual amendments under the SEA, see O.J. No L 169/01-29, 29 Jun. 1987.

\(^{83}\) Ibid, at 7-12; Section II: Provisions relating to foundations and policy of the Community. These amendments / additions introduced qualified majority voting principle to several legal bases; e.g., Art. 28, 57(2), 70(1), 84(2), 100a, 100b, 118a, 130q(2) (in conj. with 130k, 130l, 130m, 130n, 130p), 2\(^{nd}\) para of Art. 130s EEC.

\(^{84}\) See, e.g., the new provisions added to the EEC Treaty through the SEA concerning economic and monetary policy [Art. 102a(2) (in conj. with existing Art. 236 EEC)], criteria for national laws on health and safety of workers (Art 118a EEC), roles in regional development, and economic and social cohesion (Art. 130a-130e EEC), research and technological development (Art. 130f-130q EEC), environment (Art. 130r, 130s EEC), etc.

\(^{85}\) For example, harmonisation of turnover taxes, excise duties and other indirect taxes still required unanimity (Art. 99 EEC). Art. 100a EEC was newly introduced under the SEA which did not require unanimity to integrate national laws but fiscal matters (including direct taxation) were excluded from its purview (Art. 100a (2) EEC). Some of the newly added legal bases also required unanimity; e.g., Art. 130q(1) (in conj. with Art. 130i, 130o), 1\(^{st}\) para of Art. 130s EEC.

\(^{86}\) Supra note 73, at 87.

\(^{87}\) On full text of amendments under the Maastricht Treaty, see O.J. C 224/01-130, 31 Aug. 1992.

\(^{88}\) See, e.g., ibid, at 8-9; Art. 2, 3, 3a TEC. Some of the explicitly added/amended new tasks included common commercial policy, common policies in the spheres of agriculture, fisheries, transport, environment, energy and tourism; measures on movement of persons, avoidance of distortive competition, and strengthening of economic and social cohesion in the internal market (Art. 3 TEC); measures leading to the introduction of single currency (Art. 3a TEC), etc.

\(^{89}\) The Commission (supra note 57) reports that as many as twenty or so activities became open to the Community action pursuant to the Maastricht Treaty.
qualify now as Community exclusive competences.\textsuperscript{90} Yet the ‘division of labour’ – in absence of cataloguing areas of concurrent and exclusive competences – largely remained vague. Likewise, there was also no stark distinction so far as to which ‘common’ areas fell within the purview of legislative competence of the Community and where its functions were merely restricted to support and coordination without superseding Members powers.\textsuperscript{91}

In order to achieve the objectives enshrined under the Maastricht constitutional plan, (non-exclusive) spheres of the Community powers were expressly required to commensurate with precise considerations. This was attained by inaugurating principles of subsidiarity and proportionality as formal building blocks of the \textit{acquis communautaire}.\textsuperscript{92} These concepts, dynamic in character, imposed pre-conditions to justify actions to be taken by the Community as well as to overseeing the content and forms of supranational actions.\textsuperscript{93} Later, a protocol and a declaration on subsidiarity were also added to the Community law under the Treaty of Amsterdam in 1997. These codified further details on the procedure of application of the principle of subsidiarity at the time of adoption of legal acts by the Community.\textsuperscript{94} A new dimension was added to the exercise of powers in the areas of non-exclusive competences of the Community when under the Treaty of Nice in 2001, concept of ‘enhanced cooperation’ was introduced. According to this, the Community (now Union) could adopt legislation in an area of non-exclusive competence subject to consensus of minimum eight (nine under the current EU law) Members. A legislative act taken under the ‘enhanced cooperation’ clause does not have an EU-wide application; rather its jurisdictional scope is restricted only to the signatories, leaving the option open for other Members to join subsequently.\textsuperscript{95}

For the first time in the history of EU law, delimitation of competences emerged expressly in the Lisbon Treaty. The journey that started under the Treaty of Rome as international polity – founded in conventional sense with normative powers flowing from \textit{competence d’ attribution} – culminated in rather characterized ‘federal-like’ competences. Title I (\textit{Categories and Areas of Union Competence}) codified in the TFEU enlisted exclusive and shared as well as supportive and supplementary competences of the Union.\textsuperscript{97} Regardless of expressed ‘division of powers’, set out in the Lisbon Treaty, a certain degree of skepticism on the part of Members to (over-) surrender powers is also inherent to it. National reservations to loss of (undue) sovereignty to ‘federation’

\begin{footnotesize}
\begin{itemize}
\item \textsuperscript{90} See, e.g., free movement of goods (Art. 9-11EEC), elimination of customs duties between Members (Art. 12-17 EEC), setting up of the common customs tariff (Art. 18-29 EEC), elimination of quantitative restrictions between Members (Art. 30-37 EEC).
\item \textsuperscript{91} Such competences have now been categorised separately under the Lisbon Treaty where the Union is empowered to take supportive and coordinating actions in certain areas (industry, culture, tourism, sports, etc. under (Art. 6 TFEU) without superseding the Members competences (Art. 2(5) TFEU).
\item \textsuperscript{92} \textit{Supra} note 56; for details, see \textit{supra} part 3.3.
\item \textsuperscript{93} See, e.g., Commission, \textit{supra} note 57.
\item \textsuperscript{94} \textit{Supra} note 58.
\item \textsuperscript{95} For Treaty of Nice, see O.J. C 80/01, 10 Mar. 2001; for specific legal provisions on enhanced cooperation, see \textit{ibid}, Art. 27a - 27e, 40 - 40b, 43 – 43b, 44, 44a, 45 TEU, and Art. 11, 11a TEC.
\item \textsuperscript{96} Tizzano \textit{supra} note 38, at 43-45.
\item \textsuperscript{97} Exclusive competences: Customs union, devising competition rules, monetary policy of Eurozone, conservation of marine biological resources, commercial policy, international agreements (Art. 3 TFEU); shared competences: internal market, specified aspects of social policy, economic, social and territorial cohesion, agriculture and fisheries, environment, consumer protection, transport, trans-European networks, energy, freedom, security and justice, public health concerns, etc. (Art. 4 TFEU); supplementary competences: human health, industry, culture, tourism, education, administrative cooperation, etc. (Art. 6 TFEU).
\end{itemize}
\end{footnotesize}
stricto senso seem to flow from the power allocation framework. For instance, ‘obsession’ to the use
of words ‘confer’ and ‘competence’; its recurrence time and again right at the outset of the TEU and the
TFEU is suggestive of Members reservations – an attempt to delineate as precisely as possible to what and how much actually is (not) included in the EU competences. 98 In the same vein, the principle of repatriation (de-confer) – added first time to the EU law and making it lawfully possible to reverse competence – also depicts a degree of uncertainty in the Members’ attitude.99

The process of application of subsidiarity rule has also been elaborated which now also includes powers to national parliaments to issue dissenting opinions for review if they find draft legislative acts inconsistent with the principle.100 In case of disagreement between the (combined) authorized number of votes of national parliaments and the Commission on compatibility of a draft act with subsidiarity, majority of the EU legislator has been assigned the final decisive powers.101

4.2 Dynamics of power allocation in taxation

4.2.1 The initial phase

The EEC Treaty, founded generally along the lines of an international organisation, ostensibly kept direct taxes away from the purview of supranational meddling, in particular, relative to tariffs and turn over tax regimes.102 Conceivably, with no conscious policy agenda on its integration in the founding periods, the Treaty paid little attention to direct taxation. The one and only explicit mention concerning direct taxes found its place in the last chapter (General and Final Provisions) of the Community law.103 Instinctively, this reference too, commensurate with the (then) status of international convention, was nothing more than a recommendation to the Members to explore channels under international diplomatic law to avoid double taxation.

During the 1960s when the ECJ dicta had been shaping up the supremacy of the EEC Treaty,104 the indirect taxes, based on the explicit legal powers, also witnessed a couple of pioneering legislation on harmonization of turn over taxes.105 There were no analogous Community actions in the area of direct taxes observed in those times. This was due to the absence of specialized legal basis or any expressed reference to powers on direct taxes in the Community law.

98 Rossi points out this interesting ‘obsession with confer’ in the Lisbon Treaty, and cites Art. 3(6), 4(1), 5(1)
and (2) TEU; Art. 7 TFEU, etc., where the word has been repeated (see supra note 73, at 93-94). Since the word confer is essentially meant for the word competence, the analysis in hand observes a similar mania for the latter word too. The expression ‘competence’ has also been widely repeated as many as 31 times right at the outset of the Treaty of Lisbon (Art. 1-4, 6 TFEU; Art. 1, 2-5 TEU).

99 Rossi, supra note 73, at 96; the author cites Declaration No. 18 (in relation to delimitation of competences)
annexed to the Treaty of Lisbon; see also, last line of Art. 2(2) TFEU.

100 Art. 6, 7 of Protocol No. 2 to the Treaty of Lisbon (supra note 3, at 207-208).

101 If the EU legislator (55% of the members of Council or a majority of the votes in European Parliament) holds
a draft act incompatible to the subsidiarity principle, the proposal is not given further consideration (ibid, Art.
7(3)(b), at 208).

102 Unlike direct taxes, abolition of customs duties between the Members (Art. 12 – 17 EEC), and establishment
of common customs tariff (Art. 18 – 29 EEC) were amongst the most explicit supranational competences. On
similar powers to harmonise turn over taxes, excise duties, and other indirect taxes, see supra part 3.2.2.

103 Art. 220 EEC that was subsequently retained as Art. 293 TEC before being repealed under the Treaty of
Lisbon; for text of 2nd indent 293 TEC, see infra part 5.1.

104 See, e.g., supra note 78.

105 For explicit powers on indirect taxes, see supra note 44; for the pioneering legislative acts on turnover taxes,
harmonisation of legislation of Member States concerning turn over taxes (O.J. 71/1301-1303, 14 Apr. 1967).
The only legal ‘clout’ traceable in the early periods was one contained in one of the objectives set by
the Treaty. It stated that ‘the activities of the Community shall include……the approximation of the
laws of the Member States to the extent required for the proper functioning of the common
market.’ Certainly, the objective did not target direct taxes exclusively but rather it encompassed
the cohesion of all (national) laws in general to the extent of their potential adversarial impacts on
the common market. Direct taxation could therefore be considered as one of those (sub-textual)
laws which the common market objectives (inherently) might intend to approximate in due course.
Yet several factors potentially could, substantially, impede ‘deciphering’ of such (legislative) intent
relating to direct taxes. Referring to the pre-requisites postulated in part 2.1, it would necessitate
search in the EEC Treaty to find a legal basis and the (then) balancing regime (if any) to evaluate the
scope of potential Community action in this policy area.

4.2.2 ‘Tracing’ the legal basis and the balancing regime
The centrality of legal bases relevant to legislation has been signified in part 3.1. These bases
supplement and complement the competence allocations and the subsidiarity rule, though the latter
two remain superimposed on these empowering tools. Under the EEC Treaty, however, both
competence delineation as well as subsidiarity notions (together hereinafter balancing regime) were
missing. In absence of both, the available space was partly occupied by these bases. Integrally, the
legal bases had a relatively higher onus in determining the legitimacy (competence analogy) of the
Community acts. The onus increased further in having a say in regulating the exercise of powers
(subsidiarity analogy) by assigning specific forms to legislative acts. Undoubtedly, selection and
application of a particular legal basis must have remained of enormous consequences for a
Community act in a given area. The legal bases, with constitutional sanction to provide foundation to
an action, still remain integral to the legislative process; nonetheless their legal dimensions to assist
area-specific legitimacy and regulation of exercise of powers have evolved and split into specialized
provisions (under current EU law). The powers vested in the legal bases under the EEC Treaty still
remain intact (under Lisbon law) and they have close affinities to the (today’s) balancing regime, and
bolster the latter.

In the early days, justifiability and the extent of a potential Community action in the sphere of direct
taxation, to a larger degree, would thus have to be found in complementary legal basis, if any at all.
Any effort to trace a (direct) tax-specific legal base would have certainly been of no gain as the word
(direct tax) itself was missing from the Treaty. The most appropriate legal basis similar to the text
embodied in the objective cited in the preceding part could be traced nowhere but again in a general
legal base. The latter authorized to ‘issue directives for the harmonisation of such laws, regulations
or administrative rules of the Member States as directly affecting the establishment or functioning of
common market’. The script of this base was too general and assimilated aims for integration of
several (national) laws through Directives without assigning any further extent or content to the
Community action. It is evident that national rules in different policy areas, for their eventual
integration, would not require identical levels of scope and substance in the legislative acts. The

106 Art. 3(h) EEC.
107 Craig, supra note 57, at 75 argues that the milder interventions by use of directives rather than deeper ones
by regulations have been designed to foster subsidiarity The author, referring to the ECJ Case T-263/07 Estonia
v Commission (2009), and Case T-374/04 Germany v Commission (2007), states that the Courts look at
directives as an indication of subsidiarity in terms of implementation.
108 Art. 100 EEC.
(lawful) scope to expand (or restrict) the extent of taking an action under such a general legal basis could also (validly) be supplemented by other provisions of law on the same area, or even provisions for other areas of substantively similar character. Nevertheless, this could also be of not much relevance for direct taxation as no other provision, save the common market principles, from within the Treaty would come to ‘rescue’ to substantiate the magnitude of the Community intervention. Other considerations justifying the scale of potential action could also come contributors through the non-Treaty approaches – such as normative or political attitudes of Members in a given area. Ironically, this too could contribute little (justification) so far as integration of direct taxation was concerned since it remained (and still remains) as an element at the core of Members fiscal sovereignty.

So far as to how the (primitive) contours of ‘balancing regime’ and its dynamics could be traced in the early days of the Community law, and if so found, how could they potentially impact direct taxes, is demonstrated in what follows. Theoretically, there is no bar on application of the tagged general legal basis to take potential action in any field (including taxes) in the context of common market. However, the scope and substance of resulting Directive, and hence, the exercise of competence in different areas, are likely to vary widely. For instance, what would transpire if the legal basis in question is applied to adopt legislative tools to take integrative measures in three different spheres: customs tariffs, VAT and direct taxes? It plausibly evidences that the outcome of the Community act in each of the three areas would differ substantially. How could the exercise of powers vested in the same legal basis result in (three) legislative documents with sufficiently varied content having materially diverse integrating effects (for three policy sectors)? A possible response, albeit not in absolute terms, could have come from the competence allocation had it been delimited expressly in the EEC law. The difference in material scope thereby indicates that the legal base also encompasses the other ‘restrictions’ or ‘expansions’, dispersed anywhere in the law concerning the (three) areas.

It can also be thus argued that in practice, the contribution of general legal basis in determining the scale of the resulting legislative outcomes (except its Directive form) is not confined to the mandate vested in the base itself. Reasonably, it goes beyond to assimilate other provisions concerning a particular policy area to explore an optimal level of integration mandated over-all by the Treaty. This entails that at the time of application of the general legal base (say) in the area of customs tariffs, it would largely embrace all other aspects set out anywhere in the Treaty for this area, and likewise, in case of an action on VAT, the legal base would adapt accordingly to the scheme envisioned for the VAT regime, and so forth. In a way, the competences, in the early days, were in rather fluid form embedded partly in the legal bases scattered all over the law, and partly disguised under the ‘nuts and bolts’ (provisions having restrictive or expansive effect on the given policy sectors) placed anywhere in the law. The same argument, to certain degree, might also hold valid for those area-sensitive legal bases, which inherently had dualistic considerations within the given sectors (shared power analogy). Hypothetically, only those legal bases would become ‘completely independent’ to exercise powers exclusively conferred upon them which have the ability to strictly ‘shut the doors’

109 In order to determine scope of a competence, any other provision(s) relating to it can fairly be taken into account. In fact Lisbon Treaty subsequently codified this principle expressly under Art. 2(6) TFEU stating that ‘The scope and arrangements for exercising union competences shall be determined by the provisions of the Treaty relating to that area.’ Likewise, provisions relating to other areas of substantially similar in nature could also be used as a secondary parameter to determine the scope of a competence under general rule of application of laws.
and become impervious (exclusive competence analogy) to any external influence (subsidiarity analogy).

Accordingly, to integrate national laws (and so direct taxes) to the extent of achieving one of the Treaty objectives (common market), powers flowing from the applicable codified tool (legal basis) would be impacted in part, by the ‘cumulative effect’ of all other relevant provisions in the corpus of the Treaty. In this context, the determination of competences in various fields required reading the entire text of the EEC Treaty. These legal dynamics, in a way, could be construed as unrefined constituents of the (then) ‘balancing regime’ meant for limiting or extending the exercise of the Community powers. Outside the ‘constitutional’ designs, sovereignty drives together with diverse normative values of the Members in various spheres might also have contributed, in due course, to the growing division of powers. Constitutional manifestation in terms of retaining the unanimity principle for certain legal bases (including taxation) under the SEA and installation of subsidiarity rule under the Maastricht appreciably put some of the flesh on skeleton of the (then) abstract ‘balancing regime’.

4.2.3 Direct taxation at the ‘back seat’

At the time of insertion of amendments in the EEC Treaty under the SEA, some of the changes also signify the underlying intents of the lawmaker towards potential Community powers (or lack thereof) in the fiscal matters, particularly direct taxation. The legal basis meant to adopt Directives on direct taxes, which had general features to accommodate several sectors, was in a way constrained to narrow down to become applicable to fewer areas including direct taxes. The constraint was created without bringing any textual amendment in this legal base; but rather within the same segment (titled ‘approximation of laws’) of the EEC Treaty, another legal base was crafted and, in order, placed immediately next to the one considered for direct taxation. The new base, also designed somewhat general in character to enable the Community acts in multiple sectors, operated in derogation to the one empowering approximation of direct taxes. Unlike the one meant for direct taxes, the new basis was equipped with legislative ease (no unanimity rule), and could also adopt multiple legislative forms (not confined to directives). In addition, it also did not stipulate the condition of ‘directly affecting the internal market’. Thus, in the post-SEA episode, Community acts

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110 Rossi (supra note 73), in the context of absence of delimitation of powers, and that the Treaty aiming to achieve its objectives through exercise of legal basis, argues that identification of competences needs reading of the complete EEC Treaty. While agreeing to this argument, this study extends it beyond the legal basis to take into account other related provisions that may in turn impact the very scope of the legal basis itself in a given area.

111 There were evident connotations for evolution of exercise of competence as to whether an area needs unanimity or qualified majority. Similarly, retention of legislative form as Directive (for Art. 100 EEC, not for Art. 100a EEC) also hints towards a regulatory check on exercise of supranational powers. For relevant legal amendments under the SEA, see supra note 83, infra notes 115, 116 and accompanying text.

112 See supra note 56 and accompanying text.

113 Factually and textually, the powers vested in Art. 100 EEC and its general application to all laws affecting common market remained intact. However, since by insertion of new legal base Art. 100a EEC, a number of areas would automatically prefer the new base over Art. 100 EEC. The preferential value of the new legal base rests in its voting ease as well as flexibility to adapt any legal form that might not necessarily be directive. Hence after the amendment, the practical use of Art. 100 would be narrowed down to the fiscal matters only which were excluded from the purview of the new base (Art. 100a(2) EEC).

114 See Art. 100a EEC added as new legal base through amendments under the SEA (supra note 82, at 8). It was placed next to the general legal base (Art. 100) considered to be applicable to direct taxes.

115 Ibid Art. 100a(1) EEC.
in various areas would positively prefer to invoke the new basis over the existing one pursuant to the ‘convenience plan’ crafted in the former. This would render the old legal basis applicable only to those limited areas not covered by the new basis. For instance, the fiscal matters including taxation were debarred from the purview of the new basis, and a Community action in direct taxes required (and still require) the already existing general legal basis. The new legal basis also excluded indirect taxes from its purview; however, it did little to indirect tax legislation that already had a specialized legal base of its own.

Another feature of the SEA-induced changes in the EEC Treaty was that it prioritized certain areas and envisioned a time bound project for specified sectors including indirect taxes to gradually establish internal market within the near future. Direct taxation, covered under the general objective of approximation of laws, was certainly missing from this preferential time bound sectoral integration plan. The amendments inserted through the SEA were indicative of the progressive extensions to the Community powers signifying a clear ‘go-ahead scheme’ for several areas excluding direct taxes. Did it imply that the Community powers in the area of direct taxes from the Rome to the SEA remained subject to ‘inertia’? With the above analysis of amendments, and given the fact that the first ever substantive legislation on direct taxes had yet to see the daylight even after more than three decades, one possible response could have come in affirmative at that point of time. Nevertheless, a closer stock taking of the overall ‘mobility’ of competences and their growing extensions gradually adding to the Community powers in different policy spheres would make the picture clearer.

### 4.2.4 Sub-textual growth of competence

One incontrovertible assumption about the several Community powers is that to varying degrees, they originate from or are impacted by the schema of common market. As the market agenda can hardly be precluded from a range of policy sectors, hence numerous market essentials (spheres) could be added to the menu of this agenda. It is also plausible that when the Community was founded as an international polity neither all such menu items were explicated categorically nor were they designed to be readily enforceable in one-go. At one point of time (the Rome, 1957), certain items of the menu were active, while others existed as semi-active, or dormant and gradually queuing (such as act-as-needed sequence) in the undergrowth of the common market essentials. At another point (the SEA, 1987), some of those ‘due-in-queue’ were added to the ‘activation list’, leaving behind another updated ‘list-in-waiting’ to be activated later at certain optimal stage (the Maastricht, 1992), and so forth. In this context, generally all areas, in theory, had to remain inevitably mobile to varying degrees in the quest for internal market. This was also precisely the case with direct taxation that factually never ‘suffered from inertia’. It was – and to an

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116 Ibid Art. 100a(2) EEC.
117 Art. 8a EEC (in conj. with Art. 8b, 8c, 100b EEC) inserted through the SEA authorised the Community to take measures with the aim to gradually establish internal market in the sectors covered under Art. 28, 57(2), 70(1), 84(2), 100a EEC, and indirect taxes (Art. 99 EEC) till 31 Dec. 1992. Notably, Art. 100 EEC was missing from this list, and therefore direct taxation was not included in time bound objectives.
118 This is what practically transpired if one overviews from the Rome (1957) to the pre-Lisbon times (2006).
119 See, e.g., supra note 90.
120 See, e.g., supra notes 84, 85.
121 See, e.g., supra notes 88, 89.
extent still is – a matter of academic argument to locate as to where direct taxation could most likely be positioned in the ‘active, semi-active or awaiting’ items of agenda menu meant for internal market. In what follows below is a succinct depiction of some of the developments (at the Commission level) during the first three decades when *prima facie* there had been widespread dormancy (of competence) in terms of non-adoptions of any legislation in the field of direct taxes.

### A. The first period

In 1960, the Commission appointed a fiscal and financial committee to study issues concerning tax harmonization in the common market. The report of the committee (Neumark Report) was released in 1963. The report underlined the importance of removing the tax obstacles from the common market, and some of its recommendations on indirect taxes laid foundations for the adoption of initial legislative acts on turnover taxes in 1967. The report also identified several problems in direct taxes such as disparities in the base of assessment and problems of corporate tax rates, withholding tax on dividends, and double taxation, etc. The committee proposed a split-rate system (German system in force at that time) with a lower rate for dividend distribution than on retained earnings to reduce economic double taxation on dividends, elimination of withholding tax on dividends of parent subsidiary, etc. The next study of the Commission, which appeared in 1970 as Temple Report, largely focused on the examination of the case for mitigation of economic double taxation of dividends. The report examined the three prevalent systems in the (six) Members at that time: the classical system (Netherlands, Luxembourg), split-rate system (Germany), and the credit system (France, Belgium). The final proposal of the report advocated the classical system where individual and corporate taxes were independent, and the corporate tax was the same for retained and distributed earnings.

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122 Certainly, the legal dynamics or power mobility are not the only ones to ultimately determine the sequence of the so called ‘list-in-waiting’ or ‘items-now-due’ considerations. One cannot ignore political and normative factors that essentially – to varying degrees in various spheres – have their roles in surrender or retention of powers by the Members. For instance, in the question in hand (Union powers to legislate in the realm of direct taxation), Members concerns over potential sovereignty loss in fiscal matters can fairly be attributed as one major factor impacting it. The evolution of power dynamics in the Community law and the political will of the Members are not mutually exclusive; both are interdependent, and in their interplay both of them, to varying degrees, inevitably impact each other. Since this paper, as mentioned in the start, seeks to investigate supranational legislative scope of direct taxes from the perspective of competence as vested in the EU law, the political dimension has largely been left aside while analyzing the so called ‘list-in-waiting’ dynamics and alike.

123 The Commission, executive organ of the EU, is responsible for moving draft legislative proposals for their adoption to the Council. The role of the Commission is extremely important in the institutional setting and legislative history of the EU.

124 Legislation adopted in the form of Council Directive 77/799/EEC concerning mutual assistance by the competent authorities of the Member States in the field of direct taxation (O.J. L 336/15-20, 27 Dec. 1977), features procedural aspects of administrative and assistance matters, and therefore has not been considered here as a legislative tool that could bring substantive approximation in direct tax laws.

125 In 1960, the Commission appointed a Committee with Fritz Neumark in the chair to study tax harmonization. On findings of the Committee, see Report of the Fiscal and Financial Committee (Neumark Report), The EEC Reports on Tax Harmonization, an unofficial translation into English language, by Hugh Thurston (IBFD 1963).


127 *Ibid*, at 123, 139, 140.

In 1968, the Commission proposed a multilateral tax treaty for the Members which could not succeed. During the first half of the 1970s, problem of tax harmonization was examined by various ad hoc committees, in particular the Werner Committee in the backdrop of the economic and monetary union. These studies contributed to the initial legislative proposals of the Commission on direct taxes. In fact the 1970s was the decade that witnessed the highest-ever legislative proposals from the Commission on direct tax matters that remained pending before the legislator seeking its consent.

Most of these legislative proposals aborted in the due course. To mention but a couple of abortive legislative attempts indicate lack of political will as well as controversies surrounding competence (or lack thereof) for the Community to act. For instance, in 1975, the Commission submitted a proposal to adopt a Directive on harmonisation of corporate tax systems and withholding taxes. The draft proposed single corporate tax rate (45–55 per cent), a partial imputation credit system with a single rate of tax credit on distributed dividends, and 25 percent withholding tax rate on dividends (except for parent-subsidiary) in the common market. The proposal met strong opposition from the Parliament (political dimension). For the legislator, a complete harmonisation could not be attained in absence of integrated tax base (connotation that the proposal was disproportionate to powers). The proposed legislation thus could not seek approval of the legislator and was finally withdrawn by the Commission in 1990.

130 See, e.g. Luck Hinnekens, “The Uneasy Case and Fate of Article 293 Second Indent EC”, INTERTAX, vol. 37, issue 11, pp. 602-609 (2009), at 603; the author states that on 1 Jul. 1968, proposal of the Commission on Multilateral Treaty for avoidance of double taxation between the Members of the Community could not succeed as it was conceived as too broad to be acceptable (in those times).


132 During 1970s, at least six proposals of the Commission relating to direct taxes and seeking adoption as Directives remained pending with the Council; see infra note 133.


134 Ibid, Commission COM(75)392 final.


137 Communication of the Commission of the European Communities to the Council, SEC(90)601 final concerning guidelines on company taxation (1990), at 10.
Another proposal, launched by the Commission in 1976, to adopt a Directive on arbitration convention for elimination of double taxation between the associated enterprises also met almost similar fate. The proposal remained pending with the legislator for several years. The Members, sensitive to potential loss of fiscal sovereignty and looming supranational encroachment on their taxing powers, demonstrated reluctance to adopt the proposal. Finally, taking shelter under an advisory provision (now repealed) of the Community law, the Members entered into an Arbitration Convention under the international public law outside the scope of the EEC Treaty. The Commission in the end had to withdraw its legislative proposal in 1996 after twenty years of its pendency before the legislator.

The foregoing synopsis of legislative endeavours, behind the prolonged stagnation exceeding three decades, transpires the evolutionary developments of direct tax regime finding its place in the progressively growing menu for agenda (common market). Instead of going through ‘legislative inertia’, it is indicative of propensity of direct taxation ‘in search of legal space’ within the Community-specific competence dynamics complimentary to the phase of common market at a given point of time. With the related Treaty provisions textually unaltered, it was in 1990, when it ultimately ‘secured the legal space’ in limited but substantive terms. The Community powers thus extended to this realm and a couple of early legislative proposals of the Commission, awaiting sanction of the lawmaker for more than two decades since their submission, were finally adopted.

**B. The second period**

At the times when a whole new paradigm was being inducted in the framework of power dynamics under the TEC, the Commission, a few months from the adoption of Directives, appointed a high profile committee to look into the tax-induced distortions in the internal market. The recommendations of the committee (Ruding Report) appeared in 1992 and included: elimination of double taxation in several forms, a uniform withholding tax rate of 30 percent on dividends subject to waiver on appropriate tax identification, concerted action by the Commission and Members defining common policy on double tax agreements, uniform tax base, and minimum corporate tax rate of 30 percent to plug harmful effects of the ‘race to bottom’ approach.

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139 The Members, pursuant to the (then) Art. 220 EEC (equivalent to Art. 293 TEC, supra note 7), entered into an Arbitration Convention (90/436/EEC of 23 Jul. 1990) under the international diplomatic law. The instrument does not have the legal backing of the EU law. Hence, not being part of **acquis communitaire**, it is neither subject to the (Commission’s) scrutiny in terms of initiation of infringement proceedings (under Art. 258-260 TFEU) nor open to the judicial jurisdiction of the ECJ.
142 Deliberations in the Heads summit at Edinburgh on the new constitutional plan, and inauguration of subsidiarity rule in the early 1990s; see supra note 56 and accompanying text. On additional information regarding extension of competences, see supra notes 88, 89. For further developments on balancing regime in later half of the 1990s, see also supra note 58.
143 The Committee with Onno Ruding, the Dutch Finance Minister, in chair was appointed by the Commission to examine company taxation in the European Community as of 25 Oct. 1990; Ruding, infra note 144, at 7.
While most of the recommendations of the Ruding Report were seen as over-ambitious,\(^{145}\) a new impetus to the activities of the Commission in tax policy was nevertheless noticeable in the 1990s. For instance, in an attempt to cleanse the legislative agenda, some of the archaic pending proposals that in due course had largely lost relevance were withdrawn by the Commission.\(^{146}\) There was also a visible intensity in issuance of advisory communications to sensitize the Members and the Council on tax integration;\(^{147}\) comitology approach and soft law norm of the Community were set in motion (at informal meeting of the Ministers of Economic and Finance – the ECOFIN).\(^{148}\) This resulted in pioneering soft law in this field in the form of a Code of Conduct for Business Taxation to avoid practices of harmful tax competition among the Members.\(^{149}\) The ECOFIN interaction also led the Commission to revisiting the two pending legislative proposals which were later adopted as binding law in the form Directives in 2003.\(^{150}\) Despite that the 1975 proposed Directive could not seek approval mainly on the pretext of lack of common tax base, no wide-ranging initiative in this regard could be taken over time unless the late 1990s. These were the times when plans to establish common corporate tax base and removal of double taxation occupied a permanent place in the future memo of the Commission.\(^{151}\)


\(^{146}\) The proposed Arbitration Convention was withdrawn as it had lost much of the relevance (see *supra* note 139 and accompanying text); the proposal such as COM(84)404 (*supra* note 133) was much narrow in scope for the purpose of common tax base and was withdrawn (O.J. C 2/6, 4 Jan. 1997). Other withdrawals of 1990s (respectively on 13 Apr. 1993 and 9 Sep. 1992) included COM(78)340 and COM(79) 737, *supra* note 133.

\(^{147}\) See, e.g., Commission’s recommendations 94/79/EC of 21 Dec. 1993 (on the taxation of certain items of income received by non-resident in a Member State other than that in which they are resident), and 94/390/EC of 25 May 1994 (on taxation of small and medium sized enterprises); Commission’s communication COM(94)206 final (on the improvement of the fiscal environment of small and medium sized enterprises), etc.

\(^{148}\) See Commission’s report on the development of tax systems COM(96)546 final of 22 Oct. 1996. The report submitted to the ECOFIN reveals that the Commission initiated an informal discussion with the ECOFIN Ministers in meeting in Verona on 13 Apr. 1996 regarding challenges such as stability of fiscal system and realization of the single market. The ECOFIN appointed a High Level Group to consider the issues. The Group met four times to examine some of the core issues of tax policy and obtained views of the stakeholders and experts. The Committee on Economic and Monetary Affairs & Industrial policy of the EU Parliament was also taken into confidence on the developments. See, also, the Commission’s communication to the Council COM(97)564 final of 5 Nov. 1997 on a package to tackle harmful tax competition in the EU. This document was submitted subsequent to meeting with the ECOFIN in Mandorf-les-Bains on 13 Sep. 1997.

\(^{149}\) Consequent to developments *ibid*, the ECOFIN adopted a Code of Conduct for Business Taxation as of 1 Dec. 1997 to tackle the harmful tax competition among Members (O.J. C 2/3-6, 6 Jan. 1998). This was the first experience of soft law in the field of direct taxes.

\(^{150}\) The ECOFIN meeting of 1 Dec. 1997 *ibid*, also led the Commission to re-submit its draft proposal on interest-royalty directive, and also approved text of draft directive on savings. Accordingly, a proposal for the former [COM(1998)67 final of 4 Mar. 1998] was submitted to the Council. The second proposal on savings directive was delivered by the Parliament and then again by the ECOFIN in its meeting of 26-27 Nov. 2000, and based on fresh conclusions, another draft proposal for directive [COM(2001)400 final of 19 Jul. 2001] was submitted to the Council. Finally the legislation was adopted through Council Directives, *supra* notes 35, 36.

With these ‘competence standings’ dispensed by the legislature and the executive in the realm of direct taxation, the Community entered the twenty first century. However, the landscape of the power dynamics might be considered as incomplete without the judicial version on the competence allocation in this policy sphere. One significant aspect in the judicial context is the frequency of the ECJ rulings in the direct tax regime that started increasing since late 1980s and got intensive in the subsequent periods.  

Notwithstanding the disputation of jurisprudence in direct taxes by legal scholarship (part 5.3), the activity itself was suggestive of progressive shift in the ‘locus’ of tax competence in the so called flexible ‘list of menu’. In what follows may correlate the growing jurisprudence on direct taxes and changing scope for the Community to exercise powers. In their pursuit to respond to the evolutionary phase internal market goes through and the level of integration it attains, the paired mobility of the accompanying economic and fiscal essentials (areas) may turn out to be inevitable. Under these situations, either the Members have to pre-empt or respond _suo moto_ or, in case their inaction (or insufficient action) does not meet the gaps, justifiable Community intervention may be warranted. If both national and supranational enactments are non-existent or deficient, the injured parties would tend to enforce their ‘constitutional rights’ by seeking remedies through national courts. The wider goes the gap, the larger would be the number of cases contested before the courts. With markedly increased number of lawsuits in the national courts, the probability of referrals to the ECJ would increase – and hence an enhanced litigation before the ECJ. The infringement proceedings initiated by the Commission may also add to such litigation before the Court but these may also inherit similar connotations. If this argument – even marginally – qualifies to explain the increased litigation in the ECJ concerning direct taxation, it may amply uphold the premise of growing normative Community powers in direct taxation over time.

5. Why EU may use the implicit legislative powers in future?

In this Section, we take a position that in the post-2009 Europe, there is a reasonably enhanced room that ever existed since the founding days to invoke constitutional powers to legislate EU-wide income tax rules. Support for this argument is sought from at least three different sources. First and foremost is the scheme of new treaty that may be construed as implicitly enhancing the power of the EU to establish Union-wide rules on direct taxation. Secondly, the EU is facing enormous financial pressures as a consequence of its commitment to provide assistance to those Members that have incurred unsustainable debt. In these circumstances, the EU has good reason to want to intervene and ensure national tax laws are sufficiently robust to raise the revenues required to pull those Members out of debt and to protect the revenue bases of wealthier Members effectively underwriting the EU assistance. Finally, experience has shown the absence of EU rules has left the room for the ECJ to strike down important parts of national legislation on the basis of general principles. Unfettered judicial intervention without the benefit of EU legislative guidance is no longer sustainable.

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152 See, e.g., Reuven S. Avi-Yonah, “What Can the US Supreme Court and the European Court of Justice Learn from Each Other’s Tax Jurisprudence?”, in Reuven S. Avi-Yonah, James R. Hines and Michael Lang (eds) _Comparative Fiscal Federalism_, pp. 465-469 (Kluwer 2007), at 465; the author points out last twenty years, especially last five years, when the ECJ aggressively interpreted the Community law and struck down several national tax rules holding them discriminatory.
5.1 Revisiting the Lisbon Treaty

Does the Lisbon Treaty offer anything different from early treaty regimes on direct taxation? Legally speaking, the TEU and TFEU, under the Lisbon inherit same ‘textual legacy’ (of no explicit reference to direct taxes) as codified in the EEC Treaty, and transmitted to the TEC. The only difference being that the sole categorical reference (2nd indent Art. 293 TEC) to direct taxation does no longer exist. What caused the provisions to vanish? Does it carry any connotations for taxation powers, and if yes, what could they be? There is no contextual information or *inter alia* an official word available on the rationale behind the repeal. Its departure remains a mystery to legal commentators and assumptions surrounding its demise have been ongoing. The entire provision as it existed read as:

‘Member States shall, so far as is necessary, enter into negotiations with each other with a view to securing for the benefit of their nationals:

- the protection of persons and the enjoyment and protection of the rights under the same conditions as those accorded by each state to its own nationals,
- the abolition of double taxation within the Community,
- the mutual recognition of companies and firms within the meaning of second paragraph of Article 48, the retention of legal personality in the event of transfer their seat from one country to another, and possibility of mergers of companies or firms governed by laws of different countries,
- the simplification of formalities governing the reciprocal recognition and enforcement of judgements of courts and arbitration awards.’

The tax literature debates various possibilities behind the repeal of 2nd indent and the consequent implications originating therefrom. The explanations offered range from a simple slip of pen or its superfluous or inconsequential presence to the enrichment of the Union objective and powers to act on double taxation issues. One view is that the provision was ancillary in character and hence its removal is of no substantial effect as its worth had long eroded by the legal force of freedom clauses. Another argument is that with the provision gone from the law, the Union objective to achieve an internal market without double taxation grows wider since its existence in a way constrained the direct effect of the objective. Remier traces its various underlying legal facets and argues remarkable seven semantic layers of the provision. Most of the literature on the repeal, to date, takes into account 2nd indent in isolation. What follows in this part, seeks to dissect this provision from multiple dimensions and investigates its repeal within the context of fuller Article 293 TEC. In arguing the reasons behind the repeal and its potential consequences to balance of powers

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155 Art. 293 TEC had replaced earlier Art. 220 EEC; both dealt with similar legal provisions.
158 Hofmann, *supra* note 156, at 81-82.
159 Kemmeren, *supra* note 156, at 158.
160 For details, see Remier, *supra* note 156, at 88-92.
on income taxation, the analysis, as an ongoing post-Lisbon debate, is an attempt in terms of competence allocation discussed in the preceding sections, and certainly not beyond the academic dispute.

5.1.1 Art. 293 TEC – potential tangle of primary / secondary competence

Legally, the entire Art. 220 EEC (Art. 293 TEC) appeared to serve as a ‘flexible window’ whereby the Community urged the Members, in four specified areas, to negotiate among themselves to achieve ‘some integration’ beyond the EEC law. The areas included: (1) equal protection of each other’s persons and their rights, (2) abolition of double taxation, (3) recognition and retention of legal personality of corporations, and (4) mutual recognition of judicial and arbitral decisions. Just as format of any standard legal document would envisage, the inaugural chapters of the EEC Treaty comprised primary clauses whereas a chapter on ‘final and general provisions’ added at the end included the remaining, general, and subsidiary items. The provision in question was positioned in the latter chapter.

The Members, insofar as deemed necessary to achieve the four specified objectives, could negotiate to enter into bilateral or multilateral agreements. Obviously such agreements, destined to supplement the primary tasks of the Community, could be attained through instruments governed under the international public law. The ancillary character, say, set out under 1st and 3rd indents, was evident as their primary clauses were already in place in the form of main provisions prohibiting discrimination based on nationality and chapters on free movement of workers and right to establishment.161 Both 1st and 3rd indents entrusted Members additional competence to reinforce the primary actions obligated under the main clauses of the Treaty. In a way, both indents carried ‘do more’ connotations at the discretion of the Members to act under international diplomatic law to bolster the powers primarily beheld by the Community. The persuasive effects of 1st indent in the subsequent developments could be best illustrated by the Schengen acquis between some of the Members. The acquis – an instrument of international public law – supplemented the objectives of freedom of movement and prohibition of nationality-based discrimination by creating a borderless area between the signatories; it finally merged into the Community legal framework under the Amsterdam Treaty.162

Did the 2nd indent on abolishing double taxation, the issue in focus, also embodied similar secondary task to supplement certain primary Community competence in the main body of law? What follows from analysis of the initial days of the Treaty in part 4.2.2 arguably might seem to disagree with it. Such a stance on 2nd indent may look as unorthodox and contradictory to the traditional explanation as the latter argues 2nd indent as having only the subsidiary powers.163 Viewed through the lenses of

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161 See Art. 7 EEC (prohibition on nationality discrimination), Art 48-51 EEC (free movement of workers), Art. 52-58 EEC (right to establishment).
162 The Schengen Agreement was signed between five out of (then) ten Members on 14 Jun. 1985 (O.J. L 239/13-18, 22 Sep. 2000), and supplemented by Schengen Convention on 19 Jun. 1990 (O.J. L 239/19-62, 22 Sep. 2000) led to creation of borderless area between the signatories. The instrument governed under the international public law became part of the Community law by a protocol added under the Treaty of Amsterdam (supra note 58, at 93-96).
163 See. e.g., supra note 158; see also Moris Lehner, “ EC Law and the Competence to Abolish Double Taxation”, in Wolfgang Gassner, Michael Lang and Eduard Lechner (eds) Tax Treaties and EC Law, pp. 1-13 (Kluwer 1996), at 2-3; the author refers to abundant literature in footnote 12 in conj. with footnote 5 holding similar views;
initial schema under the EEC Treaty (part 4.2.2), such a disputation might not seem invalid i.e., how could an explicit provision be assigned a task to act incremental to an implicit objective ‘buried deep down inside’ implied powers and general legal basis (to approximate any law directly affecting common market)? While the Community competence on direct taxes yet ‘undiscovered’ at the time EEC Treaty came into force, the spirit of 2nd indent might at best be presumed as a statement of the remaining character. Rather than supplementary, the 2nd indent would therefore appear to serve as a provision meant for the Members to cover one of the left over subjects ‘barely visible’ in the main clauses. An additional underlying memo of the provision could also be that the Community law urged the sovereigns to ‘benefit’ their ‘nationals’ from the looming Model Tax Convention of which all the (then) six Members were also contributory in another capacity.\textsuperscript{164} With the subsequent episodes of competence dynamics yet to unfold, the story certainly would not end here.

The four specified tasks set out under Art. 293 TEC entrusted powers upon the Members to negotiate and, to the extent of agreements, would eventually translate into instruments of international public law. A relevant question would rationally entail were the powers embodied under ‘so far as is necessary’ unlimited, and if not, what restrictions could the provision (inherently) pose. Regardless of the fact as to whether the powers had been of subsidiary or residual character, a general limit would require them to be exercised in consistence with general plan of the Community law. Secondly, those indents which expressly behold competence of secondary character, should never replace the primary Community competence set out in the main clauses but the former to act as incremental to the latter. A more significant aspect could be added to the second restriction, that is, the degree to limit the exercise of incremental powers would vary to meet the objectives. Even within the same policy area, the degree of variation to limit the exercise of powers might tend to vary over time. The variation could be demonstrated as follows.

An argument was built in the earlier analysis that the Community competences are not static and their dynamic nature stems from the ‘activity’ of items on the menu of common market agenda. Essentially, the restriction on exercise of secondary powers entrusted on Members (say, under 1st and 3rd indents) would intensify insofar as the Community exercises the corresponding primary powers or expand them to become more explicit. Likewise, the power vested in the seemingly residual character (say, of 2nd indent) to fill the gap of one of the left-over subjects would shift to pretend as subsidiary power if and when the ‘submerged’ Community powers in the related field would ‘emerge’ substantively to act by making use of a general legal basis on ‘approximation of laws’.

It could therefore, be pleaded that all the four indents were destined to have powers secondary in character but to varying degrees and also variably manifestable at a given point of time. An inevitable inverse relationship therefore existed between the exercise of Community powers in areas enlisted under the four indents and the secondary powers of Members to act under international public law enlisted under Art. 293 TEC. To simulate two extremes in hypothetical terms:


\footnote{Remier, \textit{supra} note 156, at 90; the author refers, in a rather different context, to the (then) ongoing efforts of another Organization for European Economic Co-operation (OEEC – the predecessor of current OECD) to develop a model tax convention in those times. The Members of the Community were part of the OEEC and also contributory to those efforts; the outcome of which appeared as first OECD Model Tax Convention on 1 Jul. 1963.}
(1) A competence of Members to enter into instruments of international public law would remain immune from Community intervention as a left-over subject if the latter decides not to ‘explore’ it ever substantively. (2) Inversely, a competence of Members flowing from amongst any of the four indents would cease to exist at all if the Community ‘explores’ and expands it to the fullest to convert it into an exclusive domain.

The history of adoption of the European arbitration convention, the only multilateral initiative of Members under the international public law pursuant to 2nd indent, unfolds a relevant but controversial episode comprising exercise of similar powers of ‘primary-secondary’ tangles. Unlike the analogous Schengen Agreement that in the spirit of 1st indent could be considered to have acted as an additional tool to bolster the right of free movement of persons, the adoption of arbitration convention outside the Community law was not free from contentious perceptions. The Members entered into the latter when the Commission’s proposed Directive on arbitration convention was pending before the Council. The commentators raised question marks on the validity of the arbitration convention as instead of supplementing the Community action, it acted to substitute the proposed legislative act. In the early days, the legal experts considered that such a convention might be derogatory to the spirit of the Community law and the Commission might contest it before the ECJ. In 2002, the Commission raised the issue to bring the convention into the folds of EC law, and also revealed its intention to issue a proposal for draft Directive in this regard but did follow it. Later, the Commission set up an EU Joint Transfer Pricing Forum and also proposed Code of Conduct on implementation of the convention but the latter is still not part of the EU law. The bottom line is that the 2nd indent, as long as it existed, hardly attained its multilateral incremental objective. Rather it would not sound out of place to argue that the controversies surrounding its past experience might have been one of the reasons of its demise. By the same token, one might also not rule out potential manipulation of legal traits of (repealed) 2nd indent to flout legitimate prospective Union actions on the pretext of Members (undue) sovereignty concerns inconsistent with the internal market imperatives.

5.1.2 Demise of Art. 293 TEC – growing reliance on EU legal order

Another possibility might also have added to vanishing of the entire provision. The instruments of international public law could play significant role in furthering the Community objectives in the early days. Two factors might be conspicuous in doing so: The Community comprised six Members, and even a bilateral agreement would in fact represent one third of them. Secondly, the legal order was not as ‘constitutinal’ as it evolved over time. Thereby in the early days, it might have been a worthy notion that potential integrative measures ‘in bits and pieces’ under the international public

165 See supra notes 139, 140 and accompanying text.
167 See, e.g., Dirk Schelpe, “The Arbitration Convention: its Origin, Its Opportunities and Its Weaknesses”, EC Tax Review, vol. 4, issue 2, pp. 68-77 (1995), at 71; the author, former Principal Administrator of the Commission, observed that ‘For the time being, .....Commission has no intention to contest the legal basis of the Arbitration Convention, but I do not exclude this in the future.’
law could also effectively bolster the Community objectives. It is quite comprehensible that with the growing Membership of the Community, the task of achieving objectives ‘in bits and pieces’ might have gone relatively difficult. The evolution of European legal order parting the ways from traditional international law also might have added further complexities to it.

If the afore-mentioned instances (Schengen and arbitration convention) are taken as specimen illustrations in achieving integration objectives outside the EU law, at least two lessons could clearly be learnt from them: First, in areas where attaining integration through unanimous or majoritarian consensus of Members proves difficult, a co-ordination of a smaller (reasonably numbered) group of Members could seize its **effet utile** in laying down foundation for an EU-wide integration (e.g., lesson from Schengen). Second, to alleviate potential complexities rising from (over-) dependence of the EC law on international public law to achieve Community objectives, the **modus operandi** of the Members powers to rely on international law needs to be channelized within the framework of EU legal system (lesson from arbitration convention). With little evidence in our hands to the contextual official documents, similar rationale could fairly be attributed to the relevant amendments to the EC law through the Amsterdam Treaty. These changes effectually added provisions that authorized a group of (minimum 51%) Members to proceed on their intended closer cooperation, and also worked out legal ‘ifs and buts’ governing such cooperation. The concept got formally ‘Europeanized’ when the provisions added under the Treaty of Nice authorized (minimum) eight Members to invoke Enhanced Cooperation. The same has also been retained in the Lisbon Treaty; where (minimum) 9 out of 27 Members (in 2009) – coincidentally the same one third strength that could do the job bilaterally in selective areas under Art. 220 EEC (in 1957) – can come together to invoke the Enhanced Cooperation clause.

Whether by default or by design, when the above amendments were being drafted under the Amsterdam Treaty, both the Schengen **acquis** and the arbitration convention, would have remained fresh in the memories of the drafters. While the former was being merged into the EC law through the Amsterdam amendments, the withdrawal of draft legislation on the latter was also notified earlier during the same year. It can therefore be argued that these amendments to the EC law rendered the four indents under Art. 293 TEC almost redundant. Going imaginatively a step ahead, the existence of the repealed clause might remotely but potentially breed connotations to act **ultra vires** to the policy and spirit of the Union law. For instance, in a hypothetical case, what implications could stem from a situation, had two or more Members agreed on a much concessionary (pre-emptive) CCCTB tool suiting them the most while acting on the basis of 2nd indent (under international public law) prior to the Commission’s legislative proposal to the Council in 2011? No doubt such an agreement could be legally contestable before the ECJ; yet a difference in hypothetically drawn comparison on (in-) validity of similar instruments of international public law between Members with and without presence of Art.293 TEC is not beyond legal comprehension.

171 *Supra* note 95.
172 Art. 326-334 TFEU.
173 *Supra* note 136 and accompanying text.
174 Commission’s proposal, *COM (2011) 121/4, 2011/0058 (CNS)* on a Common Consolidated Corporate Tax Base (CCCTB) (16 Mar. 2011); the imaginary situation presumes an action of Members prior to floating legislative proposal i.e. Members action would fulfil the so called criterion of exercise of supplementary, not substituting the Union powers as no formal legislative proposal would have been pending prior to 2011.
The repeal of expressed grant of power to Members to abolish double taxation therefore presumably seeks to avoid potential conflict of their actions (under the international public law) and that of the Union (under the EU law). Hence, the removal of the provision would seek to reinforce the EU primary (implicit) competence, in particular that on taking actions to eliminate dual or excessive tax burdens in the internal market.

5.1.3 Subsidiarity dimension
In legal terms, the repeal of 2nd indent can be interpreted to have expansionary effect on the subsidiarity test. In the preceding parts, it was observed that the repealed provision had the tendency to put a question mark as to who – the Members or the Union – had the principal competence to abolish double taxation from the internal market? If Members, under the 2nd indent, presumably had the primary power to abolish double taxation from the internal market as held by some legal scholars,\textsuperscript{175} it has gone with the repeal of the provision. Accordingly, it would mean that the supranational (secondary) competence in this area would no more be constrained by the (primary) competence held by national actors. This, in turn, would entail that action of the EU – now the sole player to act to abolishing double taxation – would be much liberally supervised by the subsidiarity check.

Conversely, if the repealed provision assigned Members supplementary integrative task, even then its demise will impact the subsidiarity function to administer the legislative scope. The repeal would reinforce the ‘signpost’ allocating a ‘give way’ connotation to the supranational action on double taxation cases pursuant to departure of controversial aspects discussed in part 5.1.1. Through indoctrinating a so called principle of \textit{absentia},\textsuperscript{176} the demise of the 2nd indent would, in any case, theoretically generate a legal space for action to prevent double taxation in the jurisdiction. The vacuum, in essence, would now be filled by the EU or, for and on its behalf, by (minimum) nine Members in the guise of enhanced cooperation clause to legislate relevant measures. Overall, this could – in the post-repeal period – now be fairly construed as to have an expansionary effect on the subsidiarity application to a Union action in policy area based otherwise on implied powers.

5.2 Growing economic compulsions
With the growing economic and fiscal constraints, there is a rising call for the EU legislature to resort to income tax policy making. Various imperatives exist that dictate this need. First, there is a lack of capacity in the domestic tax systems to individually withstand the phase internal market has reached. The single market and other surrounding sectoral legislation have attained an integration level where the implied power could be deemed to have ‘grown’ sufficiently to formulate some relevant aspects of tax policy. The sizeable growth in cross-border economic activity and the existence of a legislative void to resolve the mounting transnational disputes is evidenced from the enhanced litigation before the ECJ as argued in the concluding paragraph of part 4.2.4. Unless cohesive measures of targeted nature are adopted, the existence of diverse national legislation on income

\textsuperscript{175} See, e.g., supra note 163.

\textsuperscript{176} The parlance ‘principle of \textit{absentia}’ in its specific connotations is not being cited from the existing literature, and is being used subjectively in the given EU legal context. The principle as used here in its given framework broadly enfolds a legal principle that may infuse utilitarian or operational activism into one set of legal provisions or enhance their applicative scope – without amending it – by virtue of repeal (or \textit{absentia}) of another set of provisions in the same law.
taxation across the EU may inhibit the economic growth through adversely affecting investments and savings, and labour market.\textsuperscript{177}

Secondly, it is established that economic efficiency has links to neutrality in taxation – though the latter is unattainable in absolute terms within a national tax system.\textsuperscript{178} The same also holds valid for the EU; it means that perfect transnational neutrality in the single market would require departure from the exercise of individualistic fiscal approaches and therefore, loss of discretion over sovereign taxing powers to raise more national revenues.\textsuperscript{179} Nevertheless, an economically efficient and sustainable single market will require at least a certain degree of neutrality (approximation) of those autonomous tax policies of Members that have adversarial transnational effects. The call to address the EU-wide economic and fiscal imbalances triggered by the spill-over effects of individual approaches gets stronger during and after the crisis times.

Thirdly, though there is a little evidence that the tax policy itself generates financial crisis but there is ample evidence that it can exacerbate the economic recession.\textsuperscript{180} It can therefore be fairly argued that measures might be necessitated to curtail the contributory role of tax policy having nexus to intensify the already deteriorating economic and financial situations. In adopting such supra-state measures, the subsidiarity rule may also have accordingly fresh meanings towards the crisis-induced legislation. For instance, on the indirect taxation, the move in recent years to have a financial transaction tax (FTT) is a legislative endeavour pursuant to the financial crisis.\textsuperscript{181} Based on the enhanced cooperation clause and thus applicable to participating eleven Members when enforced,\textsuperscript{182} one could but hardly imagine any such legislation to pass the subsidiarity test ten years back.

Fourthly, evidence exists that the multinationals engage in profit shifting to low-tax jurisdictions ending up in intra-Members and intra-firms disputes of tax revenue.\textsuperscript{183} Such activities tend to erode the genuine revenue bases of national treasuries. In the wake of post-financial crisis Europe, there is an ever-increased policy demand to protect the erosion of corporate tax base in the jurisdiction. In line with the measures against base erosion and profit shifting (BEPS),\textsuperscript{184} there had been a recent move from the Commission to propose amendments in one of the existing Directives.\textsuperscript{185} However,

\textsuperscript{182} Council Decision 2013/52/EU of 22 Jan. 2013 authorizing enhanced cooperation on FTT; eleven participating Members are Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia.
\textsuperscript{184} OECD, Addressing Base Erosion and Profit Shifting (2013).
similar targeted policy responses are needed on wider range and scale to plug the loopholes of revenue leakages in the crisis-stricken dominion. In addition to protecting the corporate base to raise much needed revenue for public goods, such measures will also provide a level playing field to the honestly taxpaying firms operating across the single market.

5.3 Tax integration – judicial vs. legislative
In view of scanty legislation existing in this policy area, much of the direct tax integration to date has been achieved through rulings of the ECJ (negative integration). It is generally acknowledged that the ECJ has played – and continues to play – a vital role as the engine of overall integration in the EU. It is also historically established that the ECJ often moves in to furthering the common market objectives by filling spaces left by the ‘constitution’ drafters or the Union legislator. The ‘gap-filling’ function of the Court has an EU-specific significance in safeguarding the coherence EU legal system.

Nevertheless, there are compelling reasons for the Members to avoid judicial integration by resorting to legislative measures in this policy sector. First, notwithstanding absence in explicit terms, the implied legislative regime has attained a sufficient level where necessary laws can be enacted. In fact, the legislative gaps or lack of actions inconsistent with the obligations to uphold single market objectives have invited the traditional judicial activism to ‘formulate income tax policy in the court rooms’. For instance, the Court got itself involved in the controversial ‘tax policy making’ on dividend taxation resulting in demise of long-established imputation system from Europe.

Secondly, a conspicuous segment of legal scholarship is widely critical of the Court’s dicta on issues concerning direct taxes. According to Graetz and Warren, in absence of harmonized tax base and rate, the Court through its jurisprudence in achieving non-discriminate taxation – simultaneously both at the source and destination Member States – has stuck itself into a labyrinth of impossibility. Similarly, the Court’s approach to discrimination could also limit the Members ability to use tax policy required to stimulate their economies in the times of recession. It is quite comprehensible that exercise of multiple sovereign taxing powers in single market vis-a-vis breach of

particular tax planning arrangement (hybrid loan arrangements) and to introduce a general anti-abuse rule so that the Directive could not be exploited by tax dodgers.

Negative integration, in EU parlance, denotes removal of inconsistencies of national laws with the EU law by the ECJ rulings. Conversely, the expression positive integration refers to integration of national laws through legislatives measures.


See, e.g. ECJ’s rulings, supra note 78; see also Davies (2013), and de Witte (2011) supra note 9.


Supra note 14, at 1214-1215, 1225-1226, et seq.
freedom clauses in the EU law may generate questions of entangled judicial complexities. Such questions could however, be better responded by the Court if the intents of legislator are reflected adequately in the form of derivative statutes (Directives). Theorizing traditionally that ‘what is taking place in the Court is a kind of legislative process’, 194 or ‘witnessing a process of Europeanisation of regulation in the common market through the judicial process’ 195 might not seize comparable effet utile when it comes to rulings of the ECJ in the domain of direct taxes. 196

Thirdly, in the context of judicial harmonization of income taxation, Mclure is of the view that role of the ECJ decisions is prescriptive only i.e., it can quash or destroy (by holding national tax codes violative of the EU law) but cannot create as it does not prescribe alternate mechanisms. 197 The legislature could nevertheless do the latter. Thus attaining integration to national tax rules predominantly through prescriptive (judicial) measures instead of prescriptive (legislative) ones – at the interface of law and direct tax economics – might have adverse implications for domestic tax systems.

This so called ‘hanging sword’ of uncertainty for national treasuries, termed as ‘un-packing of settled tax systems’ by some scholars, 198 may continue to exist unless ‘the devil (laying in broad constitutional clauses) is explored in details (by secondary legislation)’. With ample authority in Union law to legislate together with growing economic imperatives to sustain single market, there is a case for unanimous consensus to recourse for having an adequate secondary tax law. The legislative path to income tax integration will also serve as a kind of quid pro quo for Members against uncertain prescriptive integration. 199

Then, irrespective of the negative integration to date and its academic disputation, there are areas that might tend to impair the single market but even the Court has refrained to intervene. 200 According to Professor Vanistendael, the Court has for instance:

- Declined to intervene cases of double tax burden resulting from application of parallel, non-discriminatory national tax rules. 201
- Assigned a wider interpretation to the rule that the Members are free to determine the allocation of taxing powers between them. 202
- Took a narrow view on the comparable tax situations of two non-resident taxpayers from different Member States. 203

195 Ibid.
196 Supra note 191 and accompanying text.
197 Mclure, supra note 4, at 408.
198 On views how the ECJ might ‘un-pack’ the established tax systems of Member, see, e.g., Kemmeren, supra note 191; on similar views capturing the demise of long established imputation system, see supra note 14, at 1208-1212.
199 Avoidance of prescriptive judicial decisions may also serve as one of the forces that could persuade states to undertake pre-emptive approaches towards measures on tax harmonization; see, e.g., Charles E. McLure Jr., “Understanding Uniformity and Diversity in State Corporate Income Taxes”, *National Tax Journal*, vol. LXI, no. 1, pp. 141–159 (2008), at 143.
201 Ibid; citing ECJ Case C-513/04 Kerckhaert-Morres.
202 Supra note 200; citing ECJ Cases C-336/96 Gilly, and C-414/06 Lidl Belgium.
It thus may not be unfounded to argue that judicial integration of national tax rules that is expected in turn to correspond optimally to single market requirements could unsurprisingly never take precedence over the one based on legislation. This is however, without prejudice to constitutional assertion of the ECJ that could not be undermined in supplementing and complementing the income taxation system in the jurisdiction – a system that otherwise should be sufficiently based on legislative actions.

6. Conclusion
Contrary to the customs and VAT, from the founding days to date, the EU law does not explicitly empower the Union to formulate income tax policy – an area left generally to Members. Nevertheless, if the national tax laws tend to infringe the internal market notion, the EU could intervene. A unique feature of the multilevel governance is that the Union-Members balance of powers is of dynamic character and changes over time in accordance with the level of integration the common market attains. As the single market grows, so do the meanings of EU competences in policy areas affecting it including the (implicit) powers in direct taxes. The study advocates that pursuant to freedom clauses, transnational economic activity has now attained a level where adequate EU-wide actions are necessitated in tax policy sector. Unless double tax burdens and other aspects of direct taxation that impede the functioning of common market are not sufficiently overcome through legislation, it is unlikely to sustain and further the idea of single market in the real economic and fiscal terms.

In the pre-Lisbon EU law, there existed an explicit grant of integrative power to Members with respect to elimination of double taxation that now stands repealed. The argument built in the study while exploring the current EU law theorizes that this repeal may actually enhance rather than diminishing the power and prospects for Union intervention. Hence there is an enhanced room for legislation in this policy area in the post-Lisbon EU law.

In addition to the enhanced scope for legislative function to formulate tax policy, the economic and financial compulsions also dictate need for supranational (legislative) intervention in the crisis-stricken jurisdiction. Then, in the wake of traditional ‘gap-filling’ function of the Court and its rulings to date on the issue at hand, a position could fairly be taken that it is in the interest of the Members to recourse to legislative tax policy. They can seize upon the opportunity to prescribe measures in the Council rather than to wait and let the ECJ to proscribe them in the court room.

203 Supra note 200; citing ECJ Cases C-376/03 D.