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THE FISCAL ANATOMY OF A
REGULATORY POLITY:
TAX POLICY AND MULTILEVEL
GOVERNANCE IN THE EU

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Tax Policy and Multilevel Governance in the EU***

ABSTRACT

The paper analyzes the common assumption that the EU has little power over taxation. We find that the EU's own taxing power is indeed narrowly circumscribed: its revenues have evolved from rather supranational beginnings in the 1950s towards an increasingly intergovernmental system. Based on a comprehensive analysis of EU tax legislation and ECJ tax jurisprudence from 1958 to 2007, we show that at the same time, the EU exerts considerable regulatory control over the member states' taxing power and imposes tighter constraints on member state taxes than the US federal government imposes on state taxation. These findings contradict the standard account of the EU as a regulatory polity which specializes in apolitical issues of market creation and leaves political issues to the member states: despite strong safeguards, the EU massively regulates the highly salient issue of member state taxation.

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The Fiscal Anatomy of a Regulatory Polity: Tax Policy and Multilevel Governance in the EU

1. WHO TAXES?

Who has taxing power in the EU? Practically all EU scholars give the same answer: only the member states! Taxes, according to Andrew Moravcsik, are largely excluded from the EU policy agenda.¹ The Member States, notes Giandomenico Majone, show a “stubborn resistance to Community interventions in areas such as ... taxation”.² Alec Stone Sweet agrees that the “EU governs principally through making rules ...; it has little capacity to govern through taxation ...”.³ James Caporaso also finds it to be “weak in terms of the traditional tax and spend functions of government”.⁴ Joseph Weiler calls the EU’s budget “laughably small”.⁵ And in Tanja Börzel’s analysis of the historical evolution of EU competencies, the EU’s tax policy competencies receive constantly low scores.⁶ Loukas Tsoukalis argues that the EU has spent an “inordinate amount of time” on tax harmonization “with rather little to show for it.”⁷ Even if harmonization occurs, EU policy is said to play only a subordinate role.⁸ Two prominent comparativists conclude that “taxation is still firmly in the hands of national governments.”⁹ We call this conventional wisdom about the EU’s tax policy abstinence the “no taxation thesis”. It has become a folk theorem of EU studies which is often stated but hardly ever tested. The purpose of our paper is to finally put it to empirical scrutiny.

The “no taxation thesis” rests on two distinct claims. First, that the EU lacks a genuine *European* tax resource, which would enable it to govern through its own financial means independently of the member states. And second, that the EU has very little control over *national* taxation and that, consequently, the member states retain substantial tax autonomy. We present supporting evidence for the first claim, by showing that despite constant calls for the introduction of an EU tax, the finances of the EU have become ever more intergovernmental over time. From fairly supranational beginnings in

¹ Moravcsik 2002, 607.

² Majone 1996a, 60.

³ Stone Sweet 2004, 239.

⁴ Caporaso, 1996, 39.

⁵ Weiler 2000, 235.

⁶ Börzel 2005, 223.

⁷ Tsoukalis 2005, 127.

⁸ Moravcsik 2005, 365.

⁹ Newton and van Deth 2005, 332.

the 1950s, the EU drifted towards a system of finance which is largely based on national contributions, controlled by the member states, and thus not fundamentally different from that of other international organizations such as the UN. We argue that the persistent failure to institute a genuine European tax resource is not just a transitional phenomenon on the way towards a fiscally empowered EU, but a structural feature likely to last. European integration does not appear to be following the precedent of advanced federal states, which invariably evolved from weak federal taxing powers in the 19th century to strong federal taxing powers in the 20th century.¹⁰

The second claim of the “no taxation thesis”, by contrast, is refuted by the evidence. Based on a comprehensive data set comprising all secondary tax legislation of the Commission and the Council of Ministers and the entire tax jurisprudence of the European Court of Justice from 1958 to 2007, we show that the tax policy choices of the Member States are increasingly embedded in and constrained by EU institutions. While it is still national governments which levy taxes, it is often the EU which determines the shape and, occasionally, even the level of taxation. This applies to all important taxes, not only indirect, but also direct taxes, albeit in different ways. The “no taxation thesis” thus misses a decisive feature of the EU tax regime: while the EU lacks taxing power in the conventional, fiscal sense, it exerts considerable regulatory power over taxation. Indeed, as a comparison will show, it subjects state taxation to stricter regulatory controls than the federal government in the United States (US).

The significance of this finding goes beyond the partial rebuttal of a widely held but rarely tested empirical assumption about the EU’s role in an obscure policy field mostly left to specialists.¹¹ Taxation is one of the constitutive powers of the modern state, and in fact its “source of life”¹². This is why Joseph Schumpeter considered public finance to be “one of the best starting points”¹³ for analyzing the logic and historical transformation of the state. It is also why Giandomenico Majone has argued that the essential starting point for understanding the EU is to acknowledge its fundamental fiscal impotence. Given the EU’s lack of an independent taxing power, Majone argues, it is constrained to govern by non-fiscal means, that is by rules and regulations. In contrast to its tax-heavy member states, it is a purely regulatory polity.¹⁴ The view of the EU gaining control of apolitical market regulation and the member states retaining control of politi-

¹⁰ E.g., McKay 2001.

¹¹ Major exceptions are Puchala 1984 and Radaelli 1997.

¹² Karl Marx cited in Campbell 1993, 164.

¹³ Schumpeter [1918] 1991, 101. Next to Schumpeter’s classic, major works in this tradition include Goldscheid 1917; Mann 1934; O’Connor 1973; Levi 1988; and Steinmo 1993.

¹⁴ Majone 1996a, 65-66.

cally salient issues of taxation, spending and other core state activities has become something like the standard model of the Euro-Polity.

Our analysis of the “no taxation thesis” has important implications for this model. It confirms that the EU is, and is likely to remain, a “regulatory polity” with little fiscal discretion as the model suggests. It also shows, however, that the substantive scope of EU regulation is much broader than the model assumes. It concerns not only highly technical matters of market governance with negligible redistributive side-effects, but also constrains the member states’ power to tax, a highly political issue of redistributive and ideological conflict. In contrast to national regulators, the EU regulates not only markets and the conduct of private market actors, but also the politics and the conduct of governments. Paradoxically, it is the purported protections of national tax autonomy (the lack of a genuine EU tax, the restricted tax policy mandate of EU institutions, and the unanimity requirement in tax harmonization) that promote restrictive European tax regulation.

In section two, we develop the standard view of the EU as a multilevel regulatory polity. Sections three and four provide empirical analyses of the two parts of the “no taxation thesis”. Section five summarizes the main findings and contrasts the tax orders of the EU and the US. Section six explores implications of our analysis for the standard regulatory polity model of the EU.

2. THE STANDARD MODEL: A MULTILEVEL REGULATORY POLITY

Since the 1990s, an increasing number of scholars have converged around the notion of the EU as a system of multilevel governance. The major advantage of this notion, and arguably one reason behind its success in EU studies, is to liberate the debate on the “nature of the beast”¹⁵ from the categorical distinctions between unconstrained national sovereignty and a European superstate, between pure intergovernmentalism and pure federalism, which had stifled it since the 1960s. Most analysts now agree that authority in the EU is neither completely monopolized by member state governments nor by EU institutions but is shared between them.¹⁶ Most authors also agree that this sharing of authority follows a specific pattern that differs markedly from the one found in Western states.

¹⁵ Risse-Kappen 1996. Major contributions to this debate include Beck and Grande 2007; Caporaso 1996; Haas 1971; Marks, Hooghe and Blank 1996; Majone 1994; Puchala 1972; Ruggie 1993; and Schmitter 1996.

¹⁶ This includes authors as diverse as Moravcsik 2005, 364 fn. 69; Hooghe and Marks, 2001; Jachtenfuchs, 2001; Leibfried and Pierson 1995; Scharpf 1999; Bache and Flinders 2004, and Kohler-Koch and Eising 1999. See Pollock 2005, 379-87 for an overview.

The key feature of the Western state is its monopoly of the legitimate use of force.¹⁷ Other features include state control of taxation, education, and large-scale redistribution.¹⁸ Systematic accounts of EU decision making powers invariably show low scores for these key policy areas:¹⁹ the EU has neither the legal mandate nor the political means for independent policy activities in defense, law and order policies, taxation, spending, or education. Decision-making in these areas is by intergovernmental agreement, tightly controlled by the member states and with little input from, and role for supranational institutions such as the European Commission, the European Parliament, or the European Court of Justice. The EU scores high, by contrast, in policy fields related to market creation (e.g., removal of barriers to movement, or monetary integration) and market regulation (e.g., occupational health and safety policies, environmental and consumer protection, or anti-trust). In these rather technical areas of low political salience, EU institutions have a broad mandate for action. Decision-making is by qualified majority voting in the Council or delegated to independent supranational bodies such as the European Commission or the European Central Bank.

These findings have congealed to what could be called the “standard model” of the Euro-Polity. The key feature of this model is a specific pattern of vertical power sharing, which different scholars describe in remarkably similar terms. According to Simon Hix “The EU is a multilevel system of government, which allows European citizens to make decisions about regulation of the continent-wide market at the European level while maintaining power over taxation and spending at the national level”.²⁰ Liesbet Hooghe and Gary Marks agree: “policies that redistribute income among individuals are handled almost exclusively within national states, whereas policies having to do with trade and market integration are handled almost exclusively at the European level.”²¹ So does Andrew Moravcsik: “The EU’s current activities are restricted by treaty and practice to a modest subset of the substantive activities pursued by the modern state. Its mandate focuses primarily on the regulation of policy externalities resulting from cross-border economic activities. [...] Absent concerns include taxation and the setting of fiscal priorities, social welfare provision, defense and police powers, education policy, cultural policy”²² and a host of other non-economic policy activities. In brief, the EU

¹⁷ Weber 1978 [1922], 54-56; Poggi 1990, 4-18.

¹⁸ C.f. Zürn and Leibfried 2005; Offe 1998, 103. See also Tilly 1985 for a historical argument.

¹⁹ The first systematic measure of decision-making authority in the EU was provided by Lindberg 1971, 69. Updates and modifications have been provided by Schmitter 1996; Börzel 2005; and Hooghe und Marks 2008.

²⁰ Hix 2008, 11.

²¹ Hooghe and Marks 2008, 115.

²² Moravcsik 2002, 607.

regulates the market and the member states do all the rest including taxes.²³ The EU is not a state, but a regulatory polity.²⁴

We do not claim that broad agreement on this standard model of vertical power sharing in the EU puts all controversy among EU scholars to rest. An important disagreement persists with respect to the relative autonomy of the different levels in the Euro-Polity. While Andrew Moravcsik in particular has argued that the member states are still in control of the EU's basic constitutional architecture,²⁵ others, like Gary Marks and Liesbet Hooghe have strongly objected to this "state-centric" claim.²⁶ We do claim, however, that there is little controversy about four major points:

- (1) Independent EU policy making is largely restricted to highly technical and politically inconspicuous issues of market regulation.
- (2) The member states retain control of highly politicized non-regulatory functions such as taxation, defense, large-scale redistribution or education.
- (3) This pattern of power sharing between the EU and the member states is normatively attractive. As the EU is not a full-blown democracy, it is patently unfit to handle politically salient conflicts of distribution or ideology. Since non-regulatory tax and spend policies are prone to such conflicts, they should be left to national governments. The EU is uniquely fit, by contrast, to handle Pareto-improving issues of market creation and regulation. These issues are largely immune to distributive conflict because they increase allocative efficiency, decrease market failure, and thus potentially benefit everyone.²⁷ Generally, voters pay little attention to them and, thus, the EU's democratic deficit is not a disadvantage. In fact, it may be advantageous, because it insulates the EU from the party politics and special interest group pressures that allegedly often corrupt regulation in national democracies.
- (4) This normatively attractive pattern of vertical power sharing is reflected in, and sustained by, Treaty restrictions on the EU's range of policy instruments (basically limited to rules and regulation), policy mandate (broad in regulation,

²³ For substantially similar accounts also see Streeck 1995, 395; Börzel 2005, 224; Hooghe and Marks 2008, 115; Héri-tier 1999; Alesina and Spolaore 2003, 210-211, and Caporaso 1996, 39.

²⁴ C.f. Majone 1996a, 1996b and 2005. In his later work, Majone has dropped his initial reference to the EU as a regulatory *state* in favor of regulatory *polity*.

²⁵ Moravcsik 1998. C.f. Pollack 2007 and Schimmelfenning 2004 for summarizing discussions of this approach.

²⁶ See in particular Marks, Hooghe and Blank 1996 and also Hooghe and Marks 2001, 2003 and 2008.

²⁷ This argument has been forcefully made by Majone 1998; Moravcsik 2002; and Scharpf 1999.

narrow in other fields) and decision making powers (high and supranational in regulation, low and intergovernmental in other fields).

Our empirical test of the “no taxation thesis” has obvious implications for this standard account of EU multilevel governance. Should we find that either EU institutions have access to independent sources of revenue or that they interfere substantially with national tax policy choices, this account would seem to require modification and normative re-evaluation.

3. NO EU TAXING POWER

At first glance, there is substantial evidence for the “no taxation thesis”. Unlike its member states, the EU has neither the legal mandate nor the administrative means to impose compulsory payments on individuals or corporations: it has no taxing power. This is not for lack of trying. The introduction of a genuine EU tax is a perennial issue in European politics. The Commission, supported by various expert panels and pro-European policy-makers, has fought for the ability to tax since the 1960s, claiming, *inter alia*, that European taxes would improve market integration, facilitate the operation of the monetary union, and bring the EU closer to the citizen by establishing a direct fiscal link to them.²⁸

Despite these efforts, the EU is no closer to having a tax of its own today than the European Coal and Steel Community (ECSC) was back in the 1950s. In fact, it is further away. As we will show, the importance of tax-like supranational levies for funding the Community budget has decreased, and the importance of national contributions has increased over time. There is a pervasive trend towards intergovernmentalism in EU finance. The so-called ‘system of own resources’ gravitates towards a funding scheme quite similar to that of international institutions such as the UN.²⁹

The ECSC Treaty of 1951 contained the seeds of a genuine European power to tax.³⁰ It empowered the High Authority to impose supranational levies on the production of coal and steel, and gave it considerable discretion to autonomously set the rate and base of levy. The levies were collected directly by the ECSC from individual coal and steel companies without any administrative assistance from the member states and thus closely resembled supranational taxes.³¹

²⁸ See e.g. Neumark Report 1963, 151; MacDougall Report 1977; European Commission 1998, 13-14; European Commission 2004, 9-12.

²⁹ E.g., Heinemann, Mohl and Osterloh 2008.

³⁰ C.f. Articles 49 and 50 of the ECSC Treaty.

³¹ Strasser 1992, 74.

The Treaty on the European Economic Community (EEC) of 1957 also provided for a supranational system of Community finance, the so-called system of “own Community resources”.³² In 1970, the Council designated customs duties and agricultural levies as the Community’s first own resources. As in the case of the ECSC levies, the rate and the base of these “traditional own resources” are set by EU institutions (in the framework of the common commercial policy and the common agricultural policy respectively), and are charged directly to certain economic agents (importers and agricultural producers), thus creating a direct, tax-like fiscal link between the Community and individual or corporate citizens. Unlike ECSC levies, the traditional own resources are collected by national rather than European authorities and pass through national budgets rather than directly to the European budget.³³ Since the agents paying customs duties or agricultural levies are mostly corporate actors, the traditional own resources failed to create the visible fiscal link between the European institutions and the European citizenship at large which the Commission and other ardent supporters of a federal Europe had longed for. Also, they serve primarily non-fiscal objectives such as trade liberalization and the stabilization of agricultural prices. It was obvious from the beginning, therefore, that they could not match the rising revenue requirements of the Community.

The Value Added Tax resource (VAT), introduced in 1979, was supposed to alleviate both problems. Envisaged as a European deduction of up to 1 per cent from national VATs (so-called “base-on-base method” because it piggy-backed the base of the European VAT resource onto the national VAT base), it would have allowed the Community to tap into a buoyant source of revenue and at the same time would have increased the Community’s profile as a revenue raiser in its own right. However, the implementation of the base-on-base method required a complete harmonization of national VAT bases because otherwise member states could have reduced their contributions to the European budget simply by curtailing their national VAT bases. While the Council achieved a substantial approximation in 1977, a complete harmonization proved elusive. This made the base-on-base approach unfeasible and tipped the scales in favor of a purely statistical approach to collecting the VAT resource (so-called “revenue method”).³⁴

The revenue method was administratively convenient but fundamentally changed the character of the VAT resource from a direct European charge on final consumers to a national contribution of the member states. Despite its name, the VAT resource is not directly linked to the VAT payments of European consumers but represents a national

³² Art. 201 EC Treaty (now Art. 269).

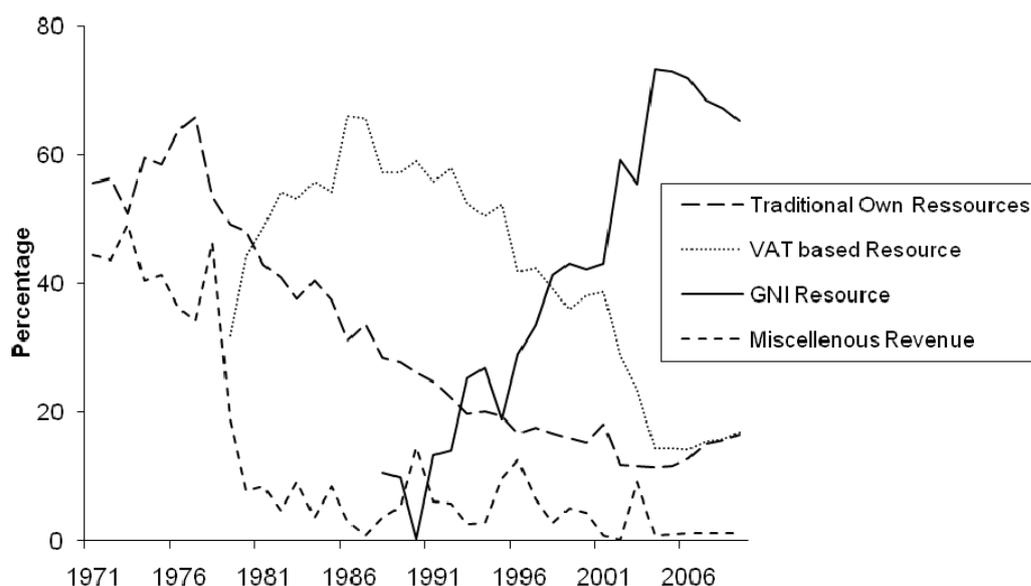
³³ Strasser 1992, 88-90.

³⁴ Genschel 2002, 80-95. Denmark used the fiscal base-on-base method until 1982, Ireland until 1985. Afterwards, all member states applied the statistical revenue method c.f. Strasser 1992, 91.

payment obligation of the member states. In essence, it is a purely statistical construct, calculated from harmonized data on aggregate national consumption, paid out of general tax revenue, and transferred to the EU in monthly installments. Critical observers consider it as “revenue dressed up as an own resource”³⁵ but not as a genuine own resource.

The introduction of the so-called Gross National Income (GNI)-resource³⁶ in 1988 reinforced the drift from supranational levies to national contributions. In contrast to the VAT resource, which at least initially was intended to have certain tax-like features, the GNI resource was conceived right from the beginning as a transfer from national treasuries. It is calculated on the basis of harmonized data on the GNI of the member states without even nominal reference to microeconomic events or actors. The GNI resource has quickly turned into the keystone of the own resource system. In 2007, it accounted for roughly 70 per cent of all own resources. Current reform trends point towards a further expansion of its role in EU finance.³⁷

Figure 1: EU Own Resources as a Percentage of Total EU Revenue, 1971-2007



Source: European Commission 2004 and <http://eur-lex.europa.eu/budget/www/index-en.htm> (last accessed Sep 27, 2009), own calculations

Figure 1 illustrates the pervasive trend in the EU’s own resources away from direct charges on individual or corporate citizens towards national contributions of the mem-

³⁵ Strasser 1992, 90; c.f. Laffan 1997, 41.

³⁶ Until 1995, this resource was calculated on the basis of the gross national product (GNP resource). Since then, it is calculated on the basis of the gross national income (GNI resource).

³⁷ E.g. Grybauskaitė 2008.

ber states, i.e., away from a genuine supranational power to tax towards an intergovernmental revenue system. In 2007, almost 85 percent of EU revenues derived from national contributions, that is, VAT and GNI resources. Only 15 percent came from tax-like traditional own resources. While the High Authority of the ECSC enjoyed considerable discretion to set and administer ECSC levies, the EU Commission can only propose rates and bases of EU own resources which then have to be adopted unanimously by the Council, ratified by the parliaments of the member states, and administered by national tax authorities.³⁸

The trend towards national contributions in EU finance is reflected in, and propelled by, concerns about inter-nation distributive justice. These concerns emerged after British entry in 1973, and almost paralyzed the EU after Margaret Thatcher demanded “our money back” in 1979.³⁹ The budget rebate for the UK solved this particular problem in 1984 but at the price of drawing other member states’ attention to their budgetary net-positions.⁴⁰ By increasing the number of net-contributors to the EU budget, consecutive rounds of enlargement further increased the salience of distributive conflicts among the member states. As a consequence, the main cleavage in European budgetary debates is not between social classes as within the member states but between states. The normative reference point is inter-nation equity and the principle of the national ability to pay as in other international institutions, not inter-person equity and the principle of the individual ability to pay as in domestic politics. This explains why there are member state specific contribution rates to the VAT resource. Next to the UK, special rates also apply to Austria, Germany, the Netherlands, and Sweden, and a base cap is granted to member states with large VAT bases.⁴¹ The increasing intergovernmentalism in the EU budget may also help to explain its relatively modest size. While in Western federal states, the huge task expansion of the federal government since the early 20th century was accompanied by a huge expansion of the federal budget,⁴² the EU’s task expansion since the early 1990s was accompanied by a stagnation of the budget.

Many observers perceive the trend towards intergovernmental EU finance as pathological. According to the Commission, it fosters “a narrow *juste retour* stance”⁴³ of the member states and deflects attention from the benefits of EU policies for Europe as a whole. A direct fiscal link between the European institutions and the citizen could help

³⁸ See Pietras 2008, 16.

³⁹ See Laffan 1997, 52.

⁴⁰ See Laffan 1997, 54.

⁴¹ See 2007/436/EC, Euratom, article 2.

⁴² See Diaz-Cayeros 2004.

⁴³ European Commission 2004, technical annex p. 41 emphasis in original.

to reduce this bias and vindicate the EU as “a Union of Member states *and* citizens”.⁴⁴ The quest for a genuine European tax continues.⁴⁵ However, its visionary appeal testifies to its lack of political plausibility. The creation of a genuine European taxing power is not on the agenda because it would bestow a degree of ‘stateness’ to the EU that seems less acceptable to governments and citizens with every round of enlargement.

4. THE EU’S REGULATORY POWER OVER TAXATION

While the EU has no taxes of its own, and is unlikely to get some any time soon, it has the power to regulate the taxes of the member states. As we will show, this power to regulate goes far beyond what is implied by the standard model of the EU as a regulatory polity.

The EU’s regulatory power over taxation derives from its competence for the Single Market. The Single Market is defined as an “area without internal frontiers in which the free movement of goods, persons, services and capital is ensured”⁴⁶. To complete this market, the EU has to intervene in national policies creating such frontiers. Since goods, persons, services, and capital constitute the major tax bases of the member states (in fact there is hardly anything else to tax), this residual European power to regulate extends to all major taxes. As we will show, the EU institutions have used this power to slowly assert considerable control: the member states continue to levy taxes but EU institutions increasingly shape them. Two instruments are particularly important in this regard: the secondary tax legislation of the Commission and the Council (see section 4.1) and the case law of the European Court of Justice (see section 4.2).

4.1. Secondary Tax Legislation

The founding fathers of the EEC clearly understood that market integration requires tax policy coordination,⁴⁷ but were concerned to keep the EU’s legislative authority limited in this area. The EC Treaty gives some law making powers to EU institutions but imposes strict functional and procedural constraints on them. Functionally, it premises EU tax legislation on the needs of market integration. It mandates the Council to harmonize national tax laws for one purpose only: to ensure the proper functioning of the Single Market.⁴⁸ The fiscal and distributive considerations which animate most domestic tax

⁴⁴ European Commission 2004, 58, emphasis in original.

⁴⁵ See, e.g., Le Cacheux 2007, European Commission 2004; Cattoir 2004.

⁴⁶ Art. 14 TEC.

⁴⁷ Spaak Bericht 1956, 66-67.

⁴⁸ Art. 93 and 94 TEC. Art. 157 (3) TEC even explicitly prohibits the introduction of Community tax provisions for

Table 1: The secondary tax legislation¹ of the EU, 1958-2007

	1958-1967	1968-1977	1978-1987	1988-1997	1998-2007
by tax area					
VAT	2	6.5 ²	24	79	94.5
Excise	0	7.5	15	30	65.5
Corporate tax	0	0	0	2	3
Personal Income tax	0	0	0	0	11
Administrative Cooperation and miscellaneous tax	0	6	2	9	25
by legal instrument					
Regulations	0	0	0	8	13
Directives	2	19	35	35	39
Decisions	0	1	6	77	147
by issuing institution					
Council	2	20	41	109	179
Commission	0	0	0	11	20
Total tax legislation	2	20	41	120	199

Source: Eur-Lex, own calculations

Notes: ¹secondary tax legislation refers to binding legislative acts of the Council or the Commission concerning the national tax policy of the member states. Non-binding recommendations, opinions, etc. are not included. Also not included are binding acts concerning the customs code, state aid law or own resources. ²Some directives pertain to VAT and excises alike, for example directives on tax exemptions for individual travelers. They have been counted as 0.5 against each of these taxes.

policy debates are thus systematically excluded from the European tax policy agenda.⁴⁹ Procedurally, the Treaty subjects tax matters to unanimous decision-making. Each member state enjoys veto power over all acts of European tax legislation including those serving legitimate purposes of market integration.⁵⁰ In contrast to many other policy fields, proposals to introduce qualified majority voting in taxation were invariably struck down by sovereignty-minded member states. Arguably, taxation is now the policy field with the highest degree of intergovernmentalism in decision-making, at least in the first pillar of the EU.⁵¹ Apparently, some governments have a strong desire to keep the EU's influence over taxation weak. However, this has not prevented a strong growth

the purpose of improving the competitiveness of European industry.

⁴⁹ Of course, once a market integration rationale has been established for tax harmonization, other policy considerations also come into play (see e.g. European Commission 2001a). Importantly, however, they cannot formally justify tax harmonization. Note, however, that Art. 175 TEC empowers the Council to unanimously adopt “provisions primarily of a fiscal nature” for purposes of environmental protection.

⁵⁰ Art. 93; 95 (1); and 190 (5) TEC.

⁵¹ Börzel 2005, 222-23.

of secondary tax legislation. Table 1 gives an overview of all binding secondary tax acts ever issued by EU institutions. It highlights four trends.

First, the production of secondary tax law has greatly increased. While the Community of Six issued only two tax acts in its first decade, the EU of 15 and later of 25 member states passed almost 200 tax acts between 1998 and 2007. Despite strict functional and procedural Treaty constraints, the adoption of secondary tax law is now a routine affair in EU politics.

Second, the number of tax areas covered by secondary tax law has increased. In the 1960s, the focus of EU tax legislation was exclusively on the introduction of a common VAT system.⁵² In the 1970s and 1980s, EU tax legislation extended to excises. The Council agreed on common rules for indirect tax exemptions for individual travelers,⁵³ and for tobacco taxation⁵⁴, and also made its first cautious advance into regulating the administrative cooperation among national tax authorities.⁵⁵ In the 1990s, it entered the corporate tax field by passing two directives on the taxation of multinational companies.⁵⁶ In 2003, EU tax legislation extended into personal income tax with the so-called savings tax directive.⁵⁷ As a result, the four major taxes (VAT, excises, personal income tax and corporate tax), which together account for roughly 85 per cent of EU-27 total tax revenue,⁵⁸ are now covered by EU tax law. However, as Table 1 also shows, the coverage is very uneven. The vast majority of secondary EU tax law concerns indirect taxation (mostly VAT and excises) while the number of direct tax acts (corporate and personal income tax) is rather low. Closer inspection reveals that the systems, base definitions, rate structures and administrative procedures of VAT and excise taxes are regulated comprehensively and in great detail while the harmonization of direct taxation remains rather sketchy.⁵⁹ The difference in coverage and detail also shows in the different length of harmonization directives. While the new VAT systems directive⁶⁰ covers 118 pages of the EU's Official Journal, all corporate tax directives⁶¹ taken together cover only sixteen pages.

⁵² See 67/2277/EEC and 67/228/EEC.

⁵³ E.g. 69/169/EEC.

⁵⁴ 72/464/EEC.

⁵⁵ 77/799/EEC.

⁵⁶ 90/434/EEC and 90/435/EEC.

⁵⁷ 2003/48/EC.

⁵⁸ Own calculations based on Eurostat 2007.

⁵⁹ For a short summary of the state of play in EU tax harmonization see Uhl 2007.

⁶⁰ 2006/112/EC.

⁶¹ 90/434/EEC; 90/435/EEC; and 2003/49/EC.

Third, the variety of legal instruments has grown. In the first thirty years of integration, the *directive* was virtually the only instrument of secondary tax legislation. As the directive is binding only with respect to the ends to be achieved but leaves some discretion as to the means by which to achieve them, it was the instrument of choice for imposing unity on widely diverging national tax regimes. Indeed, it is still the preferred instrument for major acts of tax harmonization such as the horizontal excises directive of 1992,⁶² the savings directive of 2003, the introduction of the transitional system of VAT in 1991,⁶³ or the new VAT system directive in 2006.⁶⁴ However, since the late 1980s the number of tax policy *decisions* has rapidly increased and has overtaken the number of directives in the 1990s. Decisions are mostly used to authorize specific derogations from general harmonization directives for individual member states. Given that indirect taxes are much more thoroughly harmonized than direct taxes, most of these derogations concern VAT and the major excises. In a way, they provide a safety valve against an overly restrictive harmonization of these taxes. The accelerated growth of tax decisions thus provides *prima facie* evidence of the increasing restrictiveness of EU tax harmonization and testifies to the high level of European involvement in national tax policy making. Finally, *regulations* have also become somewhat more common since the 1980s even though their absolute number is still quite low. Since regulations are binding both with respect to the political ends to be achieved and the means by which to achieve them, and since they are directly applicable within the national legal orders of the member states, member state governments usually avoid them in sensitive areas. In the field of taxation, they are mostly used to lay down implementing provisions for other secondary tax law, especially harmonization directives⁶⁵.

Fourth, there is a mild trend towards delegated tax legislation. While in the early decades, all tax acts emanated from the Council of Ministers, more recently a small but increasing number of decisions and regulations have been issued by the Commission. The legal basis is provided by “parent” legislation of the Council which delegates law making powers for specific purposes to the Commission. The horizontal excise directive, for example, delegates authority over some administrative aspects of the common excise system.⁶⁶ The new VAT system directive empowers the Commission to regulate

⁶² 92/12/EEC.

⁶³ 91/680/EEC.

⁶⁴ 2006/112/EC.

⁶⁵ E.g. Council Regulation (EC) No 1777/2005 of 17 October 2005 or Commission Regulation (EC) No 2023/2005 of 12 December 2005.

⁶⁶ 92/12/EEC, Art. 24.

reduced tax rates for gas, electricity and district heating.⁶⁷ While the substantive scope of delegation is limited, it is still remarkable that law-making powers are delegated at all given the member states' strong insistence on retaining tax autonomy.

In short, the evidence suggests that the frequency, coverage, and variety of tax legislation have greatly increased. A growing number of issues concerning the rate, shape and administration of national taxes are now formally decided by the Commission and the Council. However, the evidence also shows that the scope of legislation varies greatly across taxes. Indirect taxes and especially VAT and the major excises are regulated comprehensively by secondary law while direct taxation is hardly regulated at all. This does not mean, however, that direct taxation remains free of European constraints because since the mid-1980s, the ECJ has developed a large body of case law on the compatibility of direct tax rules with primary EU law.

4.2. ECJ Tax Jurisprudence

The legal order of the EU empowers the ECJ to review the consistency of national law, including tax law, with the *acquis communautaire*. Cases can be brought by other member states, by the Commission or by private tax payers via the preliminary rulings procedure. Each tax case concerns a particular tax rule in a particular member state but the resulting case law has a harmonizing effect across taxes and member states because, by providing detailed reasons why the particular rule is (not) in line with EU law, it establishes general principles of acceptable tax policy for the EU as a whole.⁶⁸ Table 2 provides a quantitative overview of the tax jurisprudence of the ECJ. It highlights four trends.

First, the absolute number of tax cases has grown. While the ECJ handled only four tax cases between 1958 and 1967, it processed more than 400 such cases between 1998 and 2007.

Second, the number of tax areas covered has risen. For much of its history, the tax jurisprudence of the Court focused almost exclusively on indirect taxes (mostly VAT and excises). Since the 1990s, however, the number of direct tax cases (mostly concerning corporate and personal income taxes) has grown significantly. While the ECJ rendered only twenty judgments on direct taxation between 1988 and 1997, this number increased to 101 between 1998 and 2007. The relative share of direct tax cases grew from less than 10 percent of all tax cases (1988-1997) to almost 25 per cent (1998-2007). All major taxes are now under constant judicial review by the ECJ.

⁶⁷ 2006/112/EC, Art. 102.

⁶⁸ For a general treatment of this issue, see Stone Sweet 2004, 30-35.

Third, the number of cases concerning the interpretation of secondary tax law has grown much faster than those concerning primary treaty law. More than 70 percent of the cases rendered between 1998 and 2007 dealt with secondary law (292.5 out of 417). Unsurprisingly, a closer inspection reveals that this share is much higher in indirect taxation: almost 98 percent of all VAT cases between 1998 and 2007 (203 out of 208) concerned secondary VAT law. The share is much lower in direct taxation, where little secondary law exists. Only about 20 percent of the corporate tax cases (10 out of 46.5) and no case concerning personal taxes related to secondary tax law.⁶⁹ In other words, in indirect taxation the ECJ rules *on* the secondary legislation of the Council while in direct taxation it mostly rules *in lieu* of Council legislation. In the former case, the jurisprudence of the ECJ adds to the legal constraints of secondary tax legislation by clarify-

Table 2: Tax jurisprudence¹ of the ECJ, 1958-2007

	1958-1967	1968-1977	1978-1987	1988-1997	1998-2007
by tax area					
VAT	1	17	33.5 ²	116	208
Excise and other indirect tax	2	19	49.5 ²	68	102
Corporate tax	0	1	2	8	46.5 ⁴
Personal tax ³	1	2	2	12	54.5 ⁴
Administrative Cooperation and miscellaneous tax	0	0	1	5	6
by legal subject					
Primary law	4	29	56	68	124.5 ⁵
Secondary law	0	10	32	141	292.5 ⁵
by type of procedure					
Preliminary ruling	3	32	64	158	340
Infringement (failure to fulfil obligation)	1	5	24	49	68
Other	0	2	0	2	9
Total tax jurisprudence	4	39	88	209	417

Source: Eur-lex, own calculations

Notes: ¹tax jurisprudence refers to judgements of the ECJ on the compatibility of national tax law and European law. Orders as well as judgements on the EU's own resources are not included. The categorization of cases as tax jurisprudence does not follow the register of the ECJ because this register counts as tax cases only cases which have been decided on the basis of either primary tax law (the 'tax chapter' of the TEC) or secondary tax law. It thus misses many direct tax cases which have been decided on the basis of general treaty provisions on non-discrimination, the four freedoms or competition policy. ²Some judgements apply to VAT and excises. They are counted as 0.5 against each tax. ³Personal tax includes income, wealth, and inheritance taxes. ⁴Some judgements apply to corporate and personal taxes. They are counted as 0.5 against each tax. ⁵Some judgements refer to primary and secondary law. They are counted as 0.5 against each legal subject.

⁶⁹ The only exception is case C-87/99 (*Zurstrassen*) which amongst other issues dealt with the implications of the non-tax Council Regulation 1612/68/EEC for personal income taxation.

ing the meaning of this legislation and thus whittling away some of the formula compromises and ambiguities that originally secured unanimous agreement in the Council. In the latter case, it creates judge-made European tax law in a field in which the Council has traditionally refused to legislate because the member states could not or would not agree to European level rules. In other words: "While European Union governments do their best to avoid harmonizing [direct] taxation, the EU's court of justice is busy doing it for them."⁷⁰

Most direct tax cases concern the compatibility of national tax provisions with the general non-discrimination and free movement guarantees of the EC Treaty.⁷¹ Direct tax regimes are liable to violate these guarantees, as historically they were designed to ensure efficiency and distributive fairness within national boundaries rather than non-discrimination and unrestricted movement across them. Governments built up protective walls around national tax domains in order to prevent the mobile tax base from leaking out: tax advantages were limited to domestic situations, and extra tax or administrative requirements were imposed on international situations. The ECJ has taken a very critical view of these protective arrangements, and began shooting them down in the 1980s in the name of the market freedoms. An in-depth analysis of the corporate tax jurisprudence suggests that the member states lost almost three-quarters of all cases.⁷² This judicial onslaught triggered a wave of national tax reforms. Governments in Finland, France, Germany, Ireland, Italy and elsewhere eliminated the once popular but inherently discriminatory imputation system of corporate taxation. Also, domestic tax advantages were extended to cross-border situations or eliminated altogether in order to preempt anti-discrimination litigation. Indirectly, the ECJ's tax jurisprudence also affected national tax rates because it fuelled corporate tax competition in the Single Market by eliminating tax barriers to cross-border transactions.⁷³ The corporate tax jurisprudence also had important knock-on effects on personal taxation, for example in the treatment of individual wealth and capital income.⁷⁴ Most tax lawyers agree that the ECJ "strongly influences almost all aspects of company tax law"⁷⁵ and deeply affects the taxation of individual income and wealth.⁷⁶

⁷⁰ The Economist cited in Kaye 2007, 195.

⁷¹ For more detail see Terra and Wattel 2005, 27-197; Aujean 2007; and van Thiel 2007.

⁷² Genschel, Kemmerling, and Seils forthcoming, table 2

⁷³ Genschel, Kemmerling, and Seils, forthcoming.

⁷⁴ C.f. Terra and Wattel 2005, ch. 3.

⁷⁵ European Commission 2001b, 307.

⁷⁶ See e.g. Aujean 2007; van Thiel 2007; Terra and Wattel 2005, ch. 3.

Fourth, Table 2 shows that the tax jurisprudence of the ECJ is driven by two types of proceedings, references for preliminary rulings and infringement procedures. Preliminary rulings have always outnumbered infringement procedures by a significant margin. In recent years (1998-2007), the ratio has been five to one (340 to 68). The predominance of the preliminary rulings procedure gives the tax litigation before the ECJ a tax reduction bias because private tax payers will incur the costs of litigation only if they expect that a success will reduce their tax bill.⁷⁷ To the extent that private litigants are successful in their actions, they lend encouragement to other potential litigants to follow their example. Thus, successful litigation begets more litigation and increases constraints on national tax autonomy. Infringement proceedings are almost invariably initiated by the Commission. The Commission uses these proceedings primarily to ensure member state compliance with existing EU law, but also to create new law. By targeting tax obstacles which the member states refuse to remove by way of legislative harmonization, the Commission hopes to instigate case law which removes them by way of judicial harmonization.⁷⁸ The accumulation of case law may then, in turn, facilitate consensus building on legislative harmonization.⁷⁹

5. A COMPARISON OF EU AND US MULTILEVEL GOVERNANCE IN TAXATION

How does the “no taxation thesis” stand up to empirical scrutiny? The evidence presented in this paper supports the first part of the thesis: the EU does not have a source of income that even remotely resembles a tax. Despite half a century of trying, it has not managed to come closer to gaining the fiscal independence necessary to pursue large-scale spending policies on par with central governments in national federations. If anything, the EU’s fiscal independence has decreased. The system of ‘own resources’ has become more intergovernmental rather than less. While the economic case for a larger and more self-reliant EU budget is an old one, and has become stronger with the creation of Economic and Monetary Union,⁸⁰ the political case has become weaker with each round of accessions. By increasing the heterogeneity of the member states and by raising uncertainty about future member states, enlargement has fundamentally undermined the willingness of national governments to consider more fiscal independence for EU institutions. The EU is thus likely to remain a fiscally weak entity for a long time to come.

⁷⁷ Graetz and Warren 2007, 293.

⁷⁸ European Commission 2001a, 21.

⁷⁹ Aujean 2007, 329.

⁸⁰ MacDougall Report 1977.

At first glance, there is also support for the second part of the “no taxation thesis”. The EU’s regulatory authority is narrowly circumscribed in taxation. Functionally, the EC Treaty restricts its law making mandate to matters of market integration: the Council may harmonize national taxes only to the extent necessary for the proper functioning of the Single Market, but for no other purpose. Procedurally, it submits the tax legislation of the EU to the unanimity requirement.

However, this is not the whole story. Tough Treaty restrictions notwithstanding, EU institutions have asserted considerable authority over national taxation: taxes remain national but are increasingly constrained by EU legislation and jurisprudence. To be sure, the constraining effect varies across taxes. Indirect taxes are more thoroughly regulated than direct taxes and corporate taxes more thoroughly than personal income taxes. It also varies across tax instruments. Tax systems and tax base definitions tend to be more narrowly circumscribed by European rules than tax rates. Most importantly, there are no binding European rules on maximum rates. The member states remain free to increase rates to raise more revenue even though their choice of rate structures and minimum rates is subject to legislative constraints in VAT, excises and savings taxation and competition constraints in corporate and (indirectly) personal income taxation.⁸¹ Obviously, the EU has not totally taken over tax policy making, but is deeply involved in its regulation. The “no taxation thesis” completely misses this crucial point.

To appreciate the distinctiveness of the EU’s fiscal architecture, we compared it to the US. We highlight three crucial differences. First, the US federal government has what EU institutions conspicuously lack: independent taxing power. Federal taxes accounted for 56 percent of total US tax revenue (67 percent if social security contributions are included) in 2006,⁸² and the rate, shape and administration of these taxes is under the exclusive control of the US Congress. State governments have no vote in, let alone veto power over, federal taxation. The EU’s own resources by contrast, accounted for roughly 2 percent of total EU-27 tax revenue in 2007, they resemble national contributions rather than taxes, and their rate, shape and administration is fully controlled by the member states.

Second, US federal institutions have more formal authority to regulate state taxation than do EU institutions. The functional and procedural restrictions on US federal law-making powers are softer. Functionally, the US Congress enjoys essentially unlimited authority under the Commerce Clause to regulate state taxes affecting interstate commerce.⁸³ This includes not only the power to constrain state taxation in the interest of

⁸¹ C.f. Ganghof and Genschel 2008.

⁸² OECD 2009, Table E, own calculations.

⁸³ C.f. Hellerstein 2007, 69.

interstate commerce, but also the power to constrain interstate commerce in the interest of the tax autonomy of the states. By contrast, the EU Council of Ministers' tax policy mandate is limited to market-enhancing legislation and does not include the protection of national tax autonomy. Procedurally, legislation in Congress is not subject to the unanimity requirement that governs the EU's Council of Ministers' tax decision making. Also, state governments have no direct representation in Congress and, hence, cannot interfere with, let alone block, federal legislation affecting their tax rates.⁸⁴ Finally, the US Supreme Court has clear authority under the Supremacy Clause to strike down state laws that are incompatible with the Constitution, including tax laws, on a par with the ECJ's competence to strike down national taxes.

Third, US federal institutions have used their regulatory authority over state taxation much more sparingly than EU institutions. Congress has rarely exercised its Commerce Clause power to regulate state taxes.⁸⁵ While it has recently legislated on issues such as state taxation of pension income or internet access,⁸⁶ it has never engaged in the type of general tax harmonization that is the hallmark of EU tax policy. Also unlike the EU, it has not exclusively legislated in the interest of unrestricted interstate commerce, though occasionally to lift dormant Commerce Clause restrictions on state taxation. The Mobile Telecommunications Sourcing Act is a case in point. In essence, it authorizes states to tax mobile phone calls that might otherwise escape taxation as result of dormant Commerce Clause jurisprudence.⁸⁷ Similarly, the US Supreme Court has treated state taxes much more leniently under the US Constitution than the ECJ has treated national taxes under the EC Treaty. Oftentimes, it has simply refused to hear cases concerning state taxation – something the ECJ cannot do. At other times, it has exercised “an extra dose of judicial sympathy for state taxing power”⁸⁸ – something the ECJ has typically been unwilling to do. While the ECJ has consistently refused to accept the revenue requirements of the member states as a valid justification for national tax provisions impinging upon the Single Market,⁸⁹ the Supreme Court has paid considerable deference to the tax policy needs of state governments, and only struck down the most egregious cases of discriminatory state tax laws.⁹⁰

⁸⁴ C.f. McLure 2007, 139.

⁸⁵ C.f. McLure 2007, 134.

⁸⁶ C.f. Kaye 2007, 206-210.

⁸⁷ C.f. Fox and Swain 2007, 625.

⁸⁸ Laurence Tribe cited in Kaye 2007, 225.

⁸⁹ C.f. e.g. Terra and Wattel 2005, 81.

⁹⁰ C.f. Avi-Yonah 2007, 466.

Apparently, the “weak” institutions of the EU impose much stronger regulatory constraints on state taxation than the “strong” US federal government. Why? The reason for this puzzling result is that the very strength of the federal government obviates the need for strict constraints on state taxation while the weakness of EU institutions fosters it. The fiscal weight of US federal taxation reduces the *importance* of differences in state taxation for the functioning of the national market.⁹¹ In the EU, where all taxes are national, cross-national tax differences matter much more for market integration. At the same time, US federal taxation reduces the *likelihood* of differences in state taxation. The states derive roughly two-thirds of their tax revenues from tax bases “co-occupied” by federal taxes.⁹² Federal tax law therefore serves as a focal reference points for state tax legislation and provides for a considerable degree of tax homogeneity across states even in the absence of formal tax harmonization.⁹³

Finally, given the ample scope of federal authority neither Congress nor the Supreme Court is bound to approach state taxation from a narrow market integration perspective. Rather they can balance the federal interest in fiscally sovereign states against the federal interest in an integrated national market. This allows them to be lenient on economically restrictive state taxation.⁹⁴ The EU institutions, by contrast, cannot balance national tax autonomy against market integration because, as the EC Treaty makes clear, taxation is none of their business except where it affects market integration. The original idea behind this narrow policy mandate was, of course, to safeguard the member states’ autonomy in taxation. The unintended effect has been to curtail their autonomy by delegitimizing revenue considerations in European tax policy discourse. Not only has the ECJ consistently refused to accept revenue requirements as a justification for restrictive national tax provisions,⁹⁵ but national revenue interests are also usually discredited in Council negotiations as harmful “national egoism” rather than as matters of common concern. To be sure, revenue considerations are ever present and inform national bargaining positions. However, they have to be draped in arguments about market integration in order to enter into official Council negotiations. This framing biases the secondary tax legislation of the Council towards market integration and against the protection of national tax autonomy, and helps to shield redistributive implications from public scrutiny.

⁹¹ C.f. Bird 1989, 149.

⁹² C.f. Keen 1998, 460.

⁹³ E.g. Daly and Weiner 1993.

⁹⁴ C.f. e.g. Pelkmans 1988, 46.

⁹⁵ Terra and Wattel 2005, 81.

If the “height of success” in regulatory policy making is to render distributive consequences invisible,⁹⁶ then the EU’s regulatory tax policy has clearly reached the pinnacle. Its impact on national taxation is so invisible that it is regularly ignored and forgotten in domestic tax policy debate. It is thus quite common for national parties and politicians to campaign on tax policy proposals that conflict with EU law.⁹⁷ Nicolas Sarkozy, for instance, pledged to reform the structure of French VAT rates in order to make the tax more equitable and efficient just to find out, after becoming president, that he needed the consent of the other 26 member states for that.⁹⁸ A more recent example concerns the proposal of German Social Democrats in the federal election campaign of 2009 to introduce a new stock exchange turnover tax. Although the EU capital duty directive⁹⁹ prohibits such a tax, the German political debate proceeded largely as if a Social Democratic government could have introduced it unilaterally.¹⁰⁰ Even when the EU’s impact on national taxation is reflected in domestic discourse, as it is most prominently in the case of corporate tax competition, the argument is usually not about the equity and legitimacy of this impact, but about the ways and means of national adjustment to it. Thus there have been numerous, and sometimes vigorous, political debates in the member states about how much to cut national corporate tax rates to survive in (or profit from) European tax competition, but there has been hardly any debate about the desirability of tax competition *per se*, simply because the level of competition is not a decision variable of national politics. Even the largest member states cannot determine it single-handedly.¹⁰¹ We conclude that the EU’s regulatory activities in taxation are of low political salience to European voters not because they are distributively neutral or ideologically innocent, but because they defy political contestation and, hence, voter attention.

The comparison between the EU and the US highlights the essential features of the fiscal architecture of the EU: although it has no independent tax income like the US federal government, its influence on taxation is by no means as weak as the “no taxation thesis” suggests. Precisely because it lacks a tax of its own and must restrict its tax policy activity to what seems indispensable for the uncontested goal of market integration, the EU tightly constrains member state taxation. Its ‘horizontal’ regulation of member

⁹⁶ Mabbett and Schelkle 2009, 700.

⁹⁷ Uhl 2008, 565.

⁹⁸ EurActiv 2008.

⁹⁹ See 2008/7/EC: article 5, para. 2 a.

¹⁰⁰ *Frankfurter Allgemeine Zeitung*, 27 July 2009, 9.

¹⁰¹ Ganghof and Genschel 2008.

state taxing powers compensates the lack of a ‘vertical’ delegation of taxing powers to EU institutions.

6. WHAT’S WRONG WITH THE REGULATORY POLITY MODEL?

Our analysis of the “no taxation thesis” has important implications for the standard model of EU as a multilevel regulatory polity. This model assumes, first of all, that the EU is largely confined to regulatory means of policy-making. Our findings confirm that the EU focuses on regulation because it lacks autonomous taxing power. They also confirm that the focus on regulation is not a transient feature of the EU on its way towards eventual fiscal empowerment but one of its enduring attributes: there is no hint of the tax centralization that marked the historical development of advanced federal states for most of the 20th century. The EU is likely to remain a regulatory polity.

Second, the standard model claims that EU regulation is largely restricted to technical matters of efficient market governance and leaves control of politically salient matters such as taxation to the member states. Our findings are contrary to this claim. The EU has developed a substantial body of tax legislation and jurisprudence that intrudes (counter-intuitively perhaps) deeply into the tax policy of its member states - much deeper, in fact, than the US federal government generally intrudes into the taxation of US states. We conclude that EU regulation has a much broader scope than is commonly understood. From creating and controlling the common European market, it branches out into controlling and constraining European governments. While the liberalization and management of cross-border economic activities may be its purported goal, the manifest effect is the shaping of domestic redistributive policy choices.

Third, the standard model suggests that the pattern of power sharing in the EU is normatively attractive. Our findings provide reasons for doubt. They indicate that the regulatory activities of the EU are less distributively innocent than the standard model implies. They also intimate that the distributive implications of EU regulation systematically escape public scrutiny. In the tax case, at least, these implications are not politicized at the EU level because the institutions involved – the Commission, the Court, and the Council – lack the means and the mandate to raise, represent and rule on conflicts of inter-personal distribution and equity (in contrast to issues of inter-state distribution and equity). The distributive implications of EU tax regulation also escape politicization at the national level either because they are simply overlooked until they actually become felt or because they enter the political discourse as external constraints to be accepted as matters of fact and not as decision variables open to contestation and political change. As Andreas Føllesdal and Simon Hix remind us, the salience of a policy issue is partly

endogenous to the political process.¹⁰² The tax regulation of the EU has low salience in the minds of European voters not because it does not affect them in important ways, but because it systematically escapes political debate and contestation.

Finally, the standard model assumes that member state control of taxation and other politically salient policies is reflected in, and protected by, the EC Treaty. Again, our findings cast doubt on this assumption. To be sure, the Treaty severely constrains the EU's policy powers in taxation, denying it access to a tax resource of its own, limiting its policy mandate to matters of market integration, and subjecting its decision-making to the unanimity rule. However, these constraints fail to protect national autonomy and, in fact, contribute to its erosion.

To understand this counterintuitive result, first consider the lack of a genuine EU tax resource. Intended to deny the EU one of the most powerful instruments, and symbols, of national statehood, it unintentionally boosts the need for European tax harmonization and regulation. For, as long as taxation remains exclusively national, cross-national differences in taxation have the largest possible potential to upset the Single Market. Hence, by keeping the EU fiscally weak, it increases the demand for strong EU regulations. Next, turn to the restriction of the EU's tax policy mandate to matters of market integration. This restriction was also meant to defend national tax autonomy by excluding the fiscal and distributive aspects of taxation from EU consideration. In effect, however, it biases EU tax legislation and jurisprudence towards ignoring these aspects. This is why the ECJ persistently refuses to consider the fiscal fall-out of its tax jurisprudence and why fiscal self-interest is often denounced as a national atavism in Council negotiations. Thus the restriction of the EU's policy mandate may inadvertently increase, rather than decrease, the risk of unwanted EU constraints on national tax autonomy.

Finally, consider the unanimity rule. It is a common fallacy among policy makers and policy analysts to assume that unanimous decision making secures high policy autonomy for the member states.¹⁰³ The underlying intuition seems compelling: as long as every single member state can strike down any new Commission proposal, the autonomy of each member state is safe from EU intrusion. However, this view overlooks the constraining effect of accumulated old decisions. Legislation is indeed difficult to adopt under unanimity. But legislation once adopted is also difficult to amend, as any amendment requires repeat unanimity. Unanimous decision-making may, thus, lock the member states into a legal status quo that many, or even most, of them no longer like but cannot agree how to change. National tax autonomy is lost in the "joint decision

¹⁰² Føllesdal and Hix 2006, 546.

¹⁰³ See Ring 2008, 209-210 for instructive examples of this fallacy.

trap”.¹⁰⁴ While the effect of the trap may be mitigated by selective derogations – as we have shown, a large share of secondary tax legislation authorizes derogations from European tax law to individual member states (see table 1) – the passage of these derogations still requires a unanimous agreement of the Council, which may not always be forthcoming.

When, for example, the German government asked for a derogation from European VAT law in 2007 in order to introduce a new, allegedly more fraud-proof, system of tax collection, it was turned down and forced to continue applying the old EU-mandated system.¹⁰⁵ Note that the unanimity requirement also raises the barriers to overruling judicial decisions.¹⁰⁶ This increases the discretion of the ECJ and puts the member states at risk of being locked into a judicial reading of the law that contradicts their original legislative intent. As is well known, the barriers to a political correction of ECJ decisions are particularly high when the interpretation of Treaty provisions is concerned: Treaty amendments require unanimous intergovernmental agreement plus subsequent ratification by national parliaments. Thus, ironically, the ECJ enjoys most discretion to impose judge-made rules in precisely those policy fields in which the member states are least able to agree on common legislative rules.¹⁰⁷ The ECJ’s activities in the direct tax field provide a good example. Many tax lawyers argue that by poking holes into domestic corporate tax systems, the ECJ tries to nudge the Council into agreement on a harmonized European system.¹⁰⁸ The risk is of course, that the ECJ ends up destroying domestic tax systems while the Council remains incapable of agreeing on common European solutions.¹⁰⁹ The Council’s hesitance to embrace the Commission’s ideas for a common consolidated corporate tax base highlights this risk.¹¹⁰ Even if the Council adopted a common European system, it would do so in response to incentives set by the ECJ and not out of a genuine desire of its democratically elected members.

In conclusion, our analysis of the fiscal architecture of the EU shows a constitutional reality which substantially differs from the standard model of the EU. While the EU has not been able to acquire any autonomous taxing power, it has imposed substantial regulatory constraints on the taxing power of the member states. This regulatory encroachment took place despite the explicit desire of the member states to retain their tax

¹⁰⁴ Scharpf 1988; Scharpf 2006.

¹⁰⁵ *Frankfurter Allgemeine Zeitung*, 6 June 2007, 16; *Frankfurter Allgemeine Zeitung*, 15 May 2008, 12.

¹⁰⁶ C.f. Pollack 2003, 169-175.

¹⁰⁷ This “dual character of supranationalism” has already been observed by Weiler 1982.

¹⁰⁸ C.f. e.g. Lang 2007, 12; Aujean 2007, 330.

¹⁰⁹ C.f. Avi-Yonah 2007, 468.

¹¹⁰ European Commission 2001c, European Commission 2007

autonomy and despite the Treaty safeguards intended to protect it. In fact, these purported safeguards contributed to undermining autonomy.¹¹¹ Our findings thus contradict a state-centric reading of Europe's multilevel polity. They show that the member states have lost control, not only of policy processes, but also of constitutional developments in the EU. However, the regulatory framing of EU tax policy tends to conceal how deeply it affects national tax policy choices. The conventional wisdom according to which the EU is limited to politically inconspicuous market regulation and the member states control politically salient issues such as taxation seems in need of modification.

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¹¹¹ The same phenomenon may also be in evidence in other policy areas of high political salience such as education (Scharpf 2007, 14), health care (Martinsen and Vrangbaek 2008), or justice and home affairs (Jachtenfuchs 2005).

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