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From the Governance of National Tax Systems to Governing Through European Taxation: A Justification for the EU's Power to Levy Taxes

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I. INTRODUCTION

Since the inception of the European Economic Community, European law has shaped Member States' tax systems. Throughout its existence, European law has addressed national tax systems' negative externalities on the functioning of the European market. From the mid-1990s onwards, an additional concern has been the adverse repercussions, such as tax policy competition and tax avoidance, of the European market on national tax systems. Since the Eurozone crisis, the measures of European macroeconomic governance have moulded national tax systems to be in line with the imperatives of financial stability and sound public finances. Gradually, the evolution of EU law has resulted in a bifurcated composition of the European Union's (EU) power to tax: while the Union significantly regulates how Member States exercise national taxing powers, it lacks the authority to levy taxes to the European public purse.[1] While endowed with regulatory faculties, the EU continues to lack the traditional 'core

* University of Turku, Faculty of Law. The original draft of the chapter was presented at the 'Power to Tax in Europe' Swedish Network for Legal Studies (SNELS) conference (Stockholm, 25–26 November 2021). For useful comments on improving the chapter, I thank the participants at the conference and Johan Lindholm in particular.

[1] AJ Menéndez, 'The Purse of the Polity' in EO Eriksen (ed), *Making the European Polity. Reflexive Integration in the EU* (Routledge 2005) 187–213; P Genschel and M Jachtenfuchs, 'How the European Union Constrains the State: Multilevel Governance of Taxation' (2011) 50 *European Journal of Political Research* 293; F Wasserfallen, 'Political and Economic Integration in the EU: The Case of Failed Tax Harmonization' (2014) 52 *Journal of Common Market Studies* 420.

state power' for the collection of tax revenues.[2] In the field of tax, the EU may be portrayed as a 'legislation-centred' polity,[3] as 'law remains the central instrument for both realising integration and for allowing the Union to govern'.[4] The EU thus shares the common feature of international organisations: rather than governing by taxes – ie, using taxes for ordering socio-economic conditions – international organisations engage in the governance of taxation – ie, shaping the national exercise of taxing powers through legislative standards.[5] Therefore, the contemporary EU lacks a genuine capacity to tax.

The power to collect taxes constitutes the lifeblood of government, as there is 'no public expenditure without taxation'.[6] The EU also needs resources to finance its functions. Certainly, since the EU is a second-order polity, it can and increasingly does extract resources from Member States' treasuries. Relying on national contributions, however, incites constant distributive struggles and divisions among Member States, and governments' *juste retour* behaviour erodes the EU's problem-solving capacities and output legitimacy.[7] The Eurozone and Covid-19 crises have only aggravated the situation. During both crises, massive political demand has put pressure on the EU to deal with the disruptions. However, the policy responses, such as macroeconomic stabilisation through financial rescue packages and recovery instruments, have involved enormous monetary resources, and reaching an agreement on these issues has proven to be a perplexing exercise in intergovernmental negotiations. It appears that in the absence of the power to levy taxes, the EU cannot engage in 'mutually beneficial mobilisation of resources on a scale that is commensurate to the many crises Europe is now facing'.[8] Therefore, conferring the power to collect taxes on the EU has been envisaged as a remedy to the EU's suboptimal problem-solving performance. In the Eurozone and Covid-19 crises, calls for the European power to levy taxes have accelerated tremendously. The former crisis marked

[2] P Genschel and M Jachtenfuchs, 'Conclusion: The European Integration of Core State Powers. Patterns and Causes' in P Genschel and M Jachtenfuchs (eds), *Beyond the Regulatory Polity? The European Integration of Core State Powers* (Oxford University Press 2013).

[3] N Walker, 'Freedom, Security and Justice' in B de Witte (ed), *Ten Reflections on the Constitutional Treaty for Europe* (European University Institute 2003) 159–81.

[4] D Chalmers, M Jachtenfuchs and C Joerges, 'The Retransformation of Europe' in D Chalmers, M Jachtenfuchs and C Joerges (eds), *The End of the Eurocrats' Dream: Adjusting to European Diversity* (Cambridge University Press 2016) 9.

[5] T Rixen and B Unger, 'Taxation: A Regulatory Multilevel Governance Perspective' (2022) 16 *Regulation and Governance* 621.

[6] AJ Menéndez, 'Taxing Europe: Two Cases for a European Power to Tax (with Some Comparative Observations)' (2004) 10 *Columbia Journal of European Law* 297, 337.

[7] J Le Cacheux, 'Funding the EU Budget with a Genuine Own Resource: The Case for a European Tax' (2007) 57 *Notre Europe Studies* 16; AR Leen, 'A European Tax: The Fiscal Sovereignty of the Member States versus the Autonomy of the European Union' in DA Frenkel and C Gerner-Beuerle (eds), *Financial Crisis, Globalisation and Regulatory Reform* (ATINER 2012); I Begg, 'Future Fiscal Arrangements of the European Union' (2004) 41 *Common Market Law Review* 775.

[8] PL Lindseth, 'The Perils of "As If" European Constitutionalism' (2016) 22 *European Law Journal* 696, 701.

the breakthrough of the political idea of a European 'fiscal capacity',[9] which soon became equated with the power to levy taxes,[10] especially in the context of the latter crisis.[11] The functional considerations indeed support using taxes as a means of governing at the EU level.

Notwithstanding the functional cause for establishing the European capacity to tax, the power to levy taxes has been considered as an exclusive prerogative of the nation state. Partly because of this normative presumption, the required consensus for conferring a genuine taxing power on the EU has not been reached among Member States. Therefore, extending taxing capacities beyond the nation state needs a proper justification. This chapter considers one possible pattern of justification. In so doing, it does not start from the principles of any *sui generis* approach to the EU. Rather, it reflects on the premise that has historically legitimised taxation in national political contexts and been authoritative in allocating taxing rights horizontally between nation states. In domestic settings, the core assumption has been a functional and reciprocal relationship between taxation and economy, in which both contribute to the other's conditions of possibility and which legitimises the collection of taxes. In the international environment, the idea thrived as an influential doctrine of economic allegiance. In the 2010s, the tenet re-emerged as a guiding idea for redesigning the international tax regime, as a host of policymakers and international organisations pleaded for the taxation of economic activities where economic value is created. This chapter proposes that the EU's power to levy taxes may be examined in the light of traditional principles that have preceded the existence of the EU and gained currency over a long historical process.

The chapter elaborates the mutually enabling relationship between taxation and economy and suggests it may be meaningfully applied to justify the vertical distribution of tax-collecting powers between the EU and its Member States. Relying on the idea of a systemic connection between the power to tax and economic value creation, the chapter concludes that the EU may make a legitimate claim to tax the economic activities that its legal system, together with national systems, enables. In this unconventional polity, there is a relevant reciprocal allegiance between the EU and economic activities taking place within the internal market, and this legitimises the EU power to levy taxes. Rather than a revolutionary and adventurous act, setting up the European capacity to tax is regarded here as a belated step in the integration process that even committed

[9] President of the European Council, 'Towards a Genuine Economic and Monetary Union'. Interim Report (Brussels, 12 October 2012). More extensively, see A Iara, 'Revenue for EMU: A Contribution to the Debate on Fiscal Union' (2016) 62 *CESifo Economic Studies* 301.

[10] F Fabbrini, 'Taxing and Spending in the Euro Zone: Legal and Political Challenges Related to the Adoption of the Financial Transaction Tax' (2014) 39 *European Law Review* 155.

[11] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, 'The Next Generation of Own Resources for the EU Budget' COM(2021) 566 final.

advocates of liberal Europe lack reason to resist. In developing this argument, the chapter proceeds essentially in three steps. Section II examines the reciprocally enabling relationship between taxation and economy in the domestic context, while section III spells out how this relationship has shaped the horizontal allocation of taxing powers between countries in the international context. Section IV reflects on the EU as a value-enabling community that has a legitimate cause to extract value from the European economy it makes possible. The concluding section V recapitulates and considers the implications of the chapter's arguments.

II. RECIPROCITY BETWEEN TAXATION AND ECONOMY IN THE LIBERAL SOCIAL ORDER

In the practice of modern government, the substantive legitimacy of taxation has rested on two properties. The first embraces the acceptable functions taxes serve vis-a-vis society, while the second involves the equitable distribution of the tax burden among individuals in society. Even though the latter permeated the twentieth-century quarrels over taxation, the rationale according to which taxes are imposed constitutes a primer that legitimises the collection of taxes in the first place.[12] This section traces such a raison d'être of taxation. In doing so, it relies on a moderate premise: rather than the pervasive role of taxes in the redistributive-interventionist and Keynesian policy regime, it considers the legitimacy of the revenue-raising function of taxes. This fiscal purpose was endorsed also in the liberal model of political rule, and long before espousing the social and interventionist orientation, 'the modern state was basically a state based on taxation, the bureaucracy of the treasury the true core of its administration'.[13] The functional and systemic legitimacy of taxation was formatively articulated in the liberal context of the limited government.

For the emergence of modern taxation, the functional separation between public and private spheres within the social order was key.[14] From the seventeenth century onwards, and reaching its climax in the nineteenth century, this differentiation developed as a separation between state and society, between government and economy.[15] In the liberal social model, the market system was

[12] S Huhnholz, 'Refeudalisierung des Steuerstaates? Vorüberlegungen zu einer politischen Theorie der Steuerdemokratie' in S Boysen, A-B Kaiser and F Meinel (eds), *Verfassung und Verteilung. Beiträge zu einer Grundfrage des Verfassungsverständnisses* (Mohr Siebeck 2015) 184–85.

[13] J Habermas, *The Structural Transformation of the Public Sphere: An Inquiry into a Category of Bourgeois Society* (trans Thomas Burger) (MIT Press 1991) 17.

[14] J Schumpeter, 'Die Krise des Steuerstaats' in R Hickel (ed), *Rudolf Goldscheid/Joseph Schumpeter. Die Finanzkrise des Steuerstaats. Beiträge zur politischen Ökonomie der Staatsfinanzen* (Suhrkamp 1976) 333–40.

[15] D Grimm, 'Die Bürgerlichkeit im Recht' in D Grimm, *Recht und Staat der bürgerlichen Gesellschaft* (Suhrkamp 1987); M Loughlin, *The Idea of Public Law* (Oxford University Press 2003) 72–98.

invented as a relatively autonomous institution, and it was seen as a primary site of promoting social and economic ends. The market was considered an action sphere of private actors, which entailed a confined role for the state. It was required that government does not dictate individuals' economic goals or reshape their commercial and contractual relations, and there was an expectation that these relations be shaped by the price mechanism and market considerations. The state was also supposed to abstain from directly engaging in market activities, therefore eschewing the role as an economic actor. The government surrendering its economic agency under the liberal premise was at the heart of the process that Rudolf Goldscheid portrayed as the 'expropriation of the state'.[16] Since expropriated from its traditional financial sources, the government was compelled to establish taxes as a permanent machinery of securing revenues. Yet, while their functional separation organised the life of a polity thoroughly, the state and the economy were not insulated from each other.[17] Rather, they were mutually embedded and served as conditions for each other's reproduction. This was most evident with respect to taxation, which functioned as a nexus between public and private involvement in the creation of value within the social order.

In the modern tax state, succeeding the collapse of the feudal order, taxes were collected as financing means, and they were essential for carrying out the general purposes that legitimised the existence and operation of the state.[18] According to political thought at the time, the government's task was seen as ensuring the life, liberty and estates of individuals. In establishing the political community, individuals were seen to aspire to preserve 'their lives, liberties, and estates, which I call by the general name, "property". The great and chief end, therefore, of men's uniting into commonwealths and putting themselves under government is the preservation of their property'.[19] Without a doubt, the government's political mandate was a limited one. However, taking care of the governing duties necessitated resources, and 'governments cannot be supported without great charge, and it is fit everyone who enjoys his share of the protection should pay out of his estate his proportion for the maintenance of it'.[20] Similarly, for Thomas Hobbes, the rationale of the state was to secure peace, liberty and proprietary rights, and taxes imposed 'on the people by the sovereign power, are nothing else but the wages, due to them that hold the public sword,

[16] R Goldscheid, 'Staat, öffentlicher Haushalt und Gesellschaft. Wesen und Aufgabe der Finanzwissenschaft vom Standpunkte der Soziologie' in R Hickel (ed), *Rudolf Goldscheid/Joseph Schumpeter: Die Finanzkrise des Steuerstaats. Beiträge zur politischen Ökonomie der Staatsfinanzen* (Suhrkamp 1976) 261–69.

[17] E-W Böckenförde, 'Die Bedeutung der Unterscheidung von Staat und Gesellschaft im demokratischen Sozialstaat der Gegenwart' in E-W Böckenförde, *Recht, Staat, Freiheit* (Suhrkamp 2013).

[18] J Snape, 'The "Sinews of the State": Historical Justifications for Taxes and Tax Law' in M Bhandari (ed), *Philosophical Foundations of Tax Law* (Oxford University Press 2017) 15–21.

[19] J Locke, *Two Treatises of Government* (Hafner Publishing 1947 [1690]) 184.

[20] ibid 193.

to defend private men in the exercise of their several trades, and callings'.[21] Enforcing property rights and contractual obligations was vital for the functioning of the economy, and this was possible only under the auspices of state authority, which in turn depended on taxes.[22] In the emerging liberal social order, taxation constituted a structural core among the systemic conditions enabling private production and exchange, and it was due to taxes that the creation and reproduction of value within the economic sphere could transpire.

While taxation enables the market economy, the collection of taxes itself is dependent on the private sphere. Since taxes are imposed on economic activities and private holdings, the private domain serves as a necessary underpinning that renders fiscal extraction feasible. This dependence is the fate of the expropriated state in the Goldscheidian sense, and it provoked Joseph A Schumpeter to characterise the tax state as an economic parasite.[23] In the liberal constitutional order, endorsing private ownership and entrusting economic efforts primarily to the private sphere, the state acts in the role of an external and non-contractual party, which takes part only in the market outcomes, which happens by means of imposing taxes.[24] Therefore, the market society is a socio-legal framework within which taxation achieves its mature design, and it functions as a systemic correlative of taxation.[25] The dependence of taxation on the market economy also entails that taxes may not frustrate the value-generating potential of the private economy, as this would eradicate the very conditions on which taxation rests.[26] Furthermore, given that taxation involves an extractive intrusion into the economy, the acceptable level of taxation became a heated issue in the liberal state. From the mid-eighteenth century onwards, political economy emerged as a pervasive disciplinary framework seeking to introduce economically rational boundaries for government powers, including taxation.[27] Still, even though the constraining principles on the power to tax were sought throughout the era of liberal state formation, and vehemently so among political economists, the role of taxation in enabling the private economy remained the premise that advised not to abolish taxes but to fix their proper position in the social and economic process of value formation.

[21] Thomas Hobbes, *The English Works of Thomas Hobbes of Malmesbury*, Vol III (John Bohn 1939 [1651]) 333–34.

[22] O Asbach, 'Thomas Hobbes und die Ambivalenzen des modernen Steuerstaates' in S Huhnholz (ed), *Fiskus – Verfassung – Freiheit: Politisches Denken der öffentlichen Finanzen von Hobbes bis heute* (Nomos 2018).

[23] Schumpeter (n 14) 346.

[24] P Kirchhof, 'Die verfassungsrechtliche Rechtfertigung der Steuern' in *Steuern im Verfassungsstaat. Symposion zu Ehren von Klaus Vogel* (CH Beck 1996) 32–33.

[25] S Huhnholz, 'Was soll das heißen: "Steuerstaat"?' in W Nienhüser and U Schmiel (eds), *Ökonomie und Gesellschaft: Jahrbuch 29. Steuern und Gesellschaft* (Metropolis Verlag 2017) 29–33.

[26] J Isensee, 'Steuerstaat als Staatsform' in R Stödter and W Thieme (eds), *Hamburg. Deutschland. Europa: Beiträge zum deutschen und europäischen Verfassungs-, Verwaltungs- und Wirtschaftsrecht. Festschrift für Hans Peter Ipsen zum siebzigsten Geburtstag* (Mohr 1977) 418.

[27] M Foucault, *The Birth of Biopolitics: Lectures at the Collège de France 1978–1979* (trans Graham Burchell) (Picador 2008) 10–73.

Since taxation enables private economy and vice versa, taxes and economy stand in a mutually reinforcing relationship, operating as each other's functional counterparts.[28] The relationship of mutual reinforcement between the public and private spheres, in which taxes contribute to the conditions of the economy and the economy provides for fiscal extraction, was essential in solidifying the conception that taxes and the economy constitute a more or less integrated socio-economic structure. By the end of the nineteenth century, this model of legitimising taxes had found a distinct form and become firmly settled in the theory of public finance, as demonstrated by Lorenz von Stein's ideas. Von Stein's justification for taxation was based on the social-theoretical assumption that it is

> beyond the possible that the community could provide for individuals, also economically, the conditions for their progress, unless individuals return [to the community] a portion of the economic rewards they derive under these conditions … This is the economic principle of any human community.[29]

By means of law, this fundamental social-theoretical principle is translated into a tax system. A tax system serves as a legal framework within which the private sphere can flourish, and hence, the members of a society ought to contribute to the public purse in return. In this, von Stein sees 'the origin of the organic circuit in the innermost life of the state …: tax potential [within the private economy] enables taxation, taxation provides for administration, and administration, in turn, engenders tax potential'.[30] Therefore, the production of economic value is a circular process, structured around public and private constituents, as prefigured by the exchange theories of taxation.[31]

On the face of it, conceptualising the relationship between taxation and society as one of mutual reproduction seems to follow the outright benefit theory of taxation. The most fully developed variant of the theory prescribes individuals to pay taxes in exchange for and in proportion to the benefits they receive from the government.[32] Thus, such a theory entails a specific criterion for distributing the fiscal burden between taxpayers. Because of its distributive premises, the benefit theory became fiercely contested at the turn of the

[28] UK Preuß, 'Rechtsstaat – Steuerstaat – Sozialstaat. Eine Problemskizze' in D Deiseroth, F Hase and K-H Ladeur (eds), *Ordnungsmacht? Über das Verhältnis von Legalität, Konsens und Herrschaft* (Europäische Verlagsanstalt 1981) 47–55.

[29] L von Stein, *Lehrbuch der Finanzwissenschaft: Zweiter Teil. Erste Abteilung* (FA Brockhaus 1885) 348. Quotations from von Stein have been translated by the author. For alternative translations, see L von Stein, 'On Taxation' in RA Musgrave and AT Peacock (eds), *Classics in the Theory of Public Finance* (Macmillan 1958).

[30] von Stein, *Lehrbuch der Finanzwissenschaft*, ibid 358.

[31] See FK Mann, *Steuerpolitische Ideale: Vergleichende Studien zur Geschichte der ökonomischen und politischen Ideen und ihres Wirkens in der öffentlichen Meinung 1600–1935* (Gustav Fischer 1937) 90.

[32] L Murphy and T Nagel, *The Myth of Ownership: Taxes and Justice* (Oxford University Press 2002) 16–19.

twentieth century, and the emerging political ideas of social justice transformed real-world tax systems.[33] To begin with, tax fairness required that the fiscal burden be distributed according to the principles of equal sacrifice or ability to pay. Furthermore, taxes were increasingly and deliberately harnessed to level socio-economic conditions and redistribute resources between individuals. Finally, the taxation of personal income forcefully asserted itself and complemented the traditionally prevalent consumption taxes. The three changes were intertwined. Tax fairness and redistribution necessitated that taxes be imposed in line with the individual taxpayer's socio-economic conditions, and the taxpayer's level of income was an important personal circumstance.[34] The abstract taxpayer of the liberal legal system was to be replaced with the more socially embedded individual, whose material and personal circumstances would be given due respect. As noted by Carl Schmitt, the concepts of the emerging tax law aimed at doing 'justice to the individual reality of living conditions, in order to conceive the economic circumstances in a fair manner with respect to taxation'.[35] Under this premise, the benefit theory was discredited for either endorsing inappropriate distributive criteria or neglecting a most vital issue of distribution altogether.

It should not be ignored that a number of liberal fiscal theories are indeed affiliated with the fully developed benefit theory of taxation. Yet, the doctrine of reciprocity between taxation and economy does not, as such, entail the fully developed form of the benefit theory. Since seeking to justify fiscal extraction from society at large, it leaves the issue of tax distribution as such unresolved. However, because this conception infers the legitimacy of taxation from the structural benefits provided by the state, it endorses what could be called the collective interpretation of the benefit theory.[36] Rather than a standard for individual tax shares, the mutual reproductivity serves as a principle for justifying the collection of taxes from a collective body of individuals. For this reason, the principle allows different interpretations of how the tax burden ought to be eventually allocated between taxpayers. In fact, from the early twentieth century onwards, governments increasingly incorporated both benefit and the ability-to-pay aspects of taxation, as they sought to strike a balance between impersonal (*ad rem*) and personal taxes. The core issue was 'to what *extent* these two contrasting principles – personal or impersonal taxation – shall be recognized in

[33] J Jaakkola, 'A Democratic Dilemma of European Power to Tax: Reconstructing the Symbiosis Between Taxation and Democracy Beyond the State?' (2019) 20 *German Law Journal* 660.

[34] AJ Menéndez, *Justifying Taxes: Some Elements for a General Theory of Democratic Tax Law* (Kluwer 2001) 101–05.

[35] C Schmitt, *Über die drei Arten des rechtswissenschaftlichen Denkens* (Duncker & Humblot 2006) 51.

[36] K Vogel, 'The Justification for Taxation: A Forgotten Question' (1988) 33 *American Journal of Jurisprudence* 19, 56–58. For a critical exposition of the principle, see JM Dodge, 'Does the "New Benefit Principle" (or the "Partnership Theory") of Income Taxation Mandate an Income Tax at both the Individual and Corporate Levels?' (2004) Public Law and Legal Theory Working Paper No 118.

our tax systems'.[37] While tax systems were rearranged under the interventionist welfare state premise, taxes continued to be legitimised also with reference to the benefits they rendered possible. Rather than endorsing an exclusive doctrinal background, the emerging tax systems implemented a dual composition and allowed two separate tax philosophies to intersect.

By the twentieth century, the systemic role of taxation in the socio-economic order was firmly entrenched, and this role legitimised the collection of taxes for fiscal purposes. Taxes enable the system of law and government, which in turn serves as an institutional precondition for creating and reproducing value within the private sphere. Taxation thus extracts value from the economy whose functioning it enables. While liberal political thought was a heterogenous tradition, its efforts to conceptualise the role of taxation in the overall economic process of value creation was one of its essential contributions to discourses on taxation. However, it undeniably lost its exclusivity as tax systems were thoroughly revamped in the political framework of the welfare state.

III. JURISDICTIONAL CONGRUENCE BETWEEN ECONOMIC VALUE FORMATION AND THE POWER TO TAX

Before the twentieth century, political thought on taxation did not significantly reflect on the territorial and international extension of the power to tax. The economy was chiefly assumed to operate within national borders, and the question regarding the activities that affiliate with a particular territory and allow a national exchequer to legitimately tax these activities was left unresolved. After the First World War, the problem of allocating taxing powers between national polities emerged rapidly. The adoption of income taxes, soaring tax rates and the quest for restoring the international economic order pushed the eradication of international double taxation onto the political agenda.[38] The double tax burden was an increasingly likely outcome, as the internationalisation of economy proceeded in parallel with states retaining their national tax sovereignty, resulting in the separation of fiscal and economic geographies.[39] With the purpose of alleviating double taxation, governments sought agreement on which state had a cause to tax and which ought to relinquish its fiscal claim. The task was to segregate taxing powers so that a proper territorial pairing between

[37] AA Young, 'Personal or Impersonal Taxation?' in *Proceedings of the Annual Conference on Taxation under the Auspices of the National Tax Association*, 10–13 August (National Tax Association 1915) 337 (emphasis original).

[38] P Genschel and T Rixen, 'Settling and Unsettling the Transnational Legal Order of International Taxation' in T Halliday and G Shaffer (eds), *Transnational Legal Orders* (Cambridge University Press 2015).

[39] On this background, see R Palan, *The Offshore World: Sovereign Markets, Virtual Places, and Nomad Millionaires* (Cornell University Press 2003).

economy and taxation would follow. This resulted in a search for suitable connecting factors that could be used to trigger the state's jurisdiction to tax.

In the nineteenth century, tax liability was generally based on national citizenship. By the time international efforts against double taxation commenced, nationality had already been largely displaced by other criteria.[40] In a famous report on double taxation, commissioned by the League of Nations and drafted by four prominent economists, the authors maintained that taxation based on nationality was predicated on the idea of political allegiance between state and individual. In their critical opinion, the economists insisted that political allegiance only had marginal relevance for tax liability. In 'the modern age of the international migration of persons as well as of capital, political allegiance no longer forms an adequate test of individual fiscal obligation'.[41] The economists suggested that political allegiance be replaced with economic allegiance, conveying material and economic factors that qualify, unlike a formal criterion of nationality, as genuinely pertinent for tax liability.[42] The concept of economic allegiance adhered in part to the notion of economic belonging (*wirtschaftliche Zugehörigkeit*) introduced by Georg Schanz[43] and developed further by Ernst Blumenstein.[44] For Schanz, the most essential aspect of economic belonging was the territorial origin of wealth and income, which referred to a territory in which wealth and income were generated. The four economists also deemed the territorial source of income a key element in economic allegiance, equating the economic origin with the community whose economic life 'makes possible the yield or the acquisition of the wealth'.[45] In addition, the economists perceived the taxpayer's country of residence as an important feature of economic allegiance. What emerged from the economists' reflections were two alternative proxies for tax jurisdiction: the residence of the taxpayer and the territorial source of income. Drawing on these, the right to tax is conferred either on the state of the taxpayer's residence or the state in which the taxpayer's income is generated.

From the 1920s to the mid-1960s, international cooperation against double taxation progressed significantly in the League of Nations and in the Organisation for European Economic Co-operation (later the Organisation for Economic Co-operation and Development (OECD)). The key goal was to opt for a proper connecting factor for tax jurisdiction and to safeguard the suitable congruence between economy and the power to tax. Framed by the four

[40] W Schön, 'Taxation and Democracy' (2019) 72 *Tax Law Review* 235, 282–87.

[41] League of Nations, *Report on Double Taxation Submitted to the Financial Committee*, document E.F.S.73. F.19; 5 April 1923 (Geneva, League of Nations, 1923) part II, section 1.

[42] ibid.

[43] G Schanz, 'Zur Frage der Steuerpflicht' (1892) 9 *Finanzarchiv* 1, 4–16.

[44] E Blumenstein, 'Die Steuer als Rechtsverhältnis' in H Teschemacher et al (eds), *Beiträge zur Finanzwissenschaft: Festgabe für Georg Schanz zum 75. Geburtstag, 12. März 1928. Band II* (JCB Mohr 1928) 3–15.

[45] League of Nations, *Report on Double Taxation* (n 41) part II, section 1.

economists' preparatory work, virtually the only proxies considered were the taxpayer's residence and the origin of income. Notwithstanding the agreement on these alternatives, the negotiations were afflicted with controversies over the actual choice between them. As recounted in the literature,[46] governments' stances oscillated between residence and source taxation. The overt background for this was countries' parochial fiscal interests. Capital-exporting countries sought to benefit from investments made abroad by their residents, which pushed them to advocate residence taxation. Capital-importing countries wished to extract from investments made by non-residents, which urged them to promote source taxation. In addition, practical concerns relating to the administration of taxes were raised, and these were prompted by the fear of tax evasion. However, there were profound tax-theoretical considerations in circulation, and these played a role in shaping the international settlement on the allocation of taxing rights, which was established by the mid-1960s.

A source country's entitlement to tax is associated with benefit taxation. In more precise terms, territorial taxation draws on the collective variant of benefit taxation, as interpreted in section II.[47] Thus, rather than only relying on an abstract international law argument about states being authorised to exercise sovereign authority within their territorial borders, source country taxation is associated with considerations characteristic to tax law and the ways of legitimising taxation in a domestic setting. In the double taxation context, the benefit doctrine expands its validity from a principle of legitimising taxation vis-a-vis the economy to an allocational rule of distributing tax bases between governments.[48] Since a source country's government provides enabling conditions also for non-residents' economic activities, 'foreigners, whose activities reach some minimum threshold, should contribute to the costs of services provided by the host government'.[49] Thomas Adams, who exerted major influence on the work against double taxation, asserted that national public bodies are constitutive in the economic process and should therefore be seen as 'silent partners in every business enterprise',[50] which legitimises taxation at the source of economic

[46] S Picciotto, *International Business Taxation: A Study in Internationalization of Business Regulation* (Cambridge University Press 2013) 1–63; T Rixen, *The Political Economy of International Tax Governance* (Palgrave Macmillan 2008) 86–116; S Jogarajan, *Double Taxation and the League of Nations* (Cambridge University Press 2018).

[47] See also K Vogel, 'Worldwide vs Source Taxation of Income: A Review and Re-evaluation of Arguments (Part I)' (1988) 16 *Intertax* 216; K Vogel, 'Worldwide vs Source Taxation of Income: A Review and Re-evaluation of Arguments (Part III)' (1988) 16 *Intertax* 393, 395; P Dietsch and T Rixen, 'Tax Competition and Global Background Justice' (2014) 22 *Journal of Political Philosophy* 150, 158.

[48] RA Musgrave and PB Musgrave, 'Inter-Nation Equity' in RM Bird and JG Head (eds), *Modern Fiscal Issues: Essays in Honour of Carl S Shoup* (University of Toronto Press 1972) 70–72.

[49] MJ Graetz, 'Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies. The David R Tillinghast Lecture' (2001) 54 *Tax Law Review* 261, 298.

[50] Cited in MJ Graetz and MM O'Hear, 'The "Original Intent" of US International Taxation' (1997) 46 *Duke Law Journal* 1021, 1036.

activities. In benefit-based source taxation, a special importance was attributed to the country in which the economic value was generated as a result of entrepreneurial and productive activities.[51] The source country's privilege to impose taxes on various types of income, such as business income, was recognised in virtually all intergovernmental solutions to double taxation, and it solidified itself as a key element in the doctrine of economic allegiance.

In source country taxation, the primary proxy for aggregating income for tax purposes is the territorial origin of income. In an internationally scattered economy, this results in the geographical fragmentation of a person's tax liability. The architects of the international tax regime saw the dispersion of tax liability as a problem because they perceived it to compromise the ability-to-pay principle. Imposing taxes in line with a taxpayer's ability to pay and at a progressive scale required that the taxpayer's entire economic circumstances and total income were taken into consideration, which necessitated choosing the taxpayer as the primary unit for clustering income.[52] This was regarded inconsistent with the system of territorially fragmented tax liability, in which the category of taxpayer was less relevant for imposing taxes than the territorial source of income.[53] For this reason, a more intimately taxpayer-related proxy for tax jurisdiction was advocated. The connecting factor was found in the taxpayer's country of residence, which allowed taxation according to the taxpayer's worldwide income and at an appropriate progressive rate. This was pivotal already in the four economists' report, which relied expressly on the ability-to-pay principle and embraced residence taxation as the key method of implementing ability-to-pay taxation in an international context.[54] However, residence taxation did not figure as antithetical to economic allegiance nor to the normative tenet that taxes be paid in a country with an economy affiliated to the taxpayer.[55] Rather, also the place of residence indicated the location of the taxpayer's economic connections, and hence, it overlapped with the premise of source taxation. The economic ties of international taxpayers are many in number, not few. But since source country taxation was incapable of taking into account the taxpayer's worldwide income and accommodating inter-individual equity, as required by ability-to-pay taxation, the territorial origin of income as the exclusive connector for tax jurisdiction was not enough. Therefore, in eradicating double taxation, source and residence were both employed in the allocation of taxing rights.

[51] W Haslehner, 'Value Creation and Income Taxation: A Coherent Framework for Reform' in W Haslehner and M Lamensch (eds), *Taxation and Value Creation* (IBFD 2021) 47.

[52] W Schön, 'International Tax Coordination for a Second-Best World (Part I)' (2009) 1 *World Tax Journal* 67, 72.

[53] NH Kaufman, 'Fairness and the Taxation of International Income' (1998) 29 *Law and Policy in International Business* 145, 167–72.

[54] League of Nations, *Report on Double Taxation* (n 41) part II.

[55] J Li, J Bao and H Li, 'Value Creation: A Constant Principle in a Changing World of International Taxation' (2019) 67 *Canadian Tax Journal* 1107, 1112.

The tension between source and residence taxation reveals how the clash between the benefit and ability-to-pay principles, originally underlying the domestic discourse on taxation, shaped the international tax regime. In the formative phase of the regime, there was also tension in the separation between impersonal and personal income taxes, characteristic to national systems of taxation.[56] The former were imposed sporadically on the taxpayer's various types of income, with each tax having a separate tax rate. Because impersonal taxes were levied independently of each other, they were incapable of aggregating the taxpayer's total income for the purpose of graduated taxation. Personal taxes, in contrast, were general in a sense that they were charged on the taxpayer's combined income. In aggregating the taxpayer's entire income, personal taxes provided for taxation at a progressive rate.[57] Since impersonal taxes largely ignored the taxpayer's personal circumstances while personal taxes took them into consideration, the former were associated with benefit and the latter with ability-to-pay taxation.[58] Drawing on the connection to benefit and ability-to-pay taxation, the experts from the League of Nations maintained that regarding impersonal taxes,

> we have recognised the primary importance of the idea of origin, that is to say, the system of the assignment of income; in the case of the general or personal tax, on the contrary, we have recognised the primary importance of the idea of domicile [residence].[59]

Systemically scattered impersonal taxes could be matched with territorially fragmented source taxation, but integrated personal taxes entailed aggregate taxation by the country of residence. The demarcation between these basic categories exerted a major, even if not uninterrupted, influence on attributing different types of income to the jurisdictions of either the source country or country of residence. This stressed the nature of income tax as a 'dual thing' that must accommodate territorial as well as ability-to-pay considerations.[60] Thus, the classical tension between benefit and ability-to-pay taxation resurfaced and shaped the international tax regime.

Between the 1920s and the mid-1940s, several model conventions for alleviating double taxation were introduced by the League of Nations. In all of the

[56] See KC Wang, 'International Double Taxation of Income: Relief through International Agreement 1921–1945' (1945) 59 *Harvard Law Review* 73, 81–92; Jogarajan (n 46) 249–50.

[57] For a conceptual analysis of personal and impersonal taxes, see WH Coates, 'Double Taxation and Tax Evasion' (1925) 88 *Journal of the Royal Statistical Society* 403.

[58] JF Avery Jones, 'Sir Josiah Stamp and Double Income Tax' in J Tiley (ed), *Studies in the History of Tax Law: Volume 6* (Hart Publishing 2013) 9–10.

[59] League of Nations, *Double Taxation and Tax Evasion: Report and Resolutions Submitted by the Technical Experts to the Financial Committee*, document F.212 February 1925 (Geneva, League of Nations, 1925) part II, section 3; see also League of Nations, *Double Taxation and Tax Evasion: Report Presented by the Committee of Technical Experts on Double Taxation and Tax Evasion*, document C.216 M. 85. 1927 II (Geneva, League of Nations, 1927).

[60] Graetz and O'Hear (n 50) 1036.

models, the power to tax specifically enumerated types of income were allocated either with reference to the origin of income or the taxpayer's residence. In so doing, the models attempted to reconcile national fiscal interests and to strike a balance between benefit and ability-to-pay taxation. Importantly, the League of Nations embraced an either-or approach: a specific item of income, such as interest income, was attributed either to residence or source country. To some extent, this changed with the OECD's 1963 Model Convention.[61] Regarding some income types, the OECD also adopted an either-or approach. However, rather than granting either source country or country of residence an exclusive right to a particular income, the one and the same income could be taxed in part by the source country, in part by the country of residence. Technically, a maximum for a source country's tax rate would be agreed upon, while the country of residence would have a right to tax the same income without any upper limit, although it was expected to credit the tax imposed by the source country. For some items of income, this became a lasting element in the international tax regime. While this has been a relatively unnoticed policy shift, it is relevant for two reasons. First, it shows the intricacy of appreciating whether specific types of economic activities ought to be associated exclusively with the source country or country of residence. The same income could have an economic allegiance with multiple countries, with each country contributing to the production of the income. Thus, not only was it necessary to balance benefit and ability-to-pay taxation against each other but also the various economic and territorial connections of income. Second, the change of approach conceded that, in the case of more than one extracting treasuries, taxing the same income could be attributed to two exchequers. Economic activities could be taxed jointly across borders.

Since the turn of the millennium, the international tax regime has been fiercely criticised. It has frequently been asserted that the regime's basic principles have proven to be outdated under the conditions of globalised, financialised and digitalised economies.[62] Does this discontent suggest that the regime's underlying aspirations are becoming relics that ought to be abandoned? The answer is in the negative. Over the last 10-year period, a powerful political credo that 'profits are taxed where economic activities take place and value is created'[63] and that there ought to be a genuine 'link between taxation and where economic activity takes place'[64] has emerged. The plea has been fuelled by the jurisdictional

[61] AJ van den Tempel, *Relief from Double Taxation* (IBFD 1967) 31–34.

[62] For instance, see Graetz (n 49); ED Kleinbard, 'Stateless Income' (2011) 11 *Florida Tax Review* 700; R Mason, 'The Transformation of International Tax' (2020) 114 *American Journal of International Law* 353, 357 and references therein.

[63] Organization for Economic Co-operation and Development, Explanatory Statement, OECD/G20 Base Erosion and Profit Shifting Project (OECD 2015) 4.

[64] Communication from the Commission to the European Parliament and the Council, 'A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action' COM(2015) 302 final, 6.

mismatch between taxation and economy. Even in a long-term perspective, this features as one of the most powerful articulations of economic allegiance, and one that has influenced the OECD's and the EU's efforts to address tax avoidance and the digitalisation of business. In academia, similar insights have been put forward, albeit under somewhat different conceptualisations.[65] These approaches to the international tax regime, and corporate tax in particular, have been informed by the aspirations of economic allegiance and the reciprocity between taxation and economy. The international tax regime's key flaw is found in its incapacity to implement, at the level of legal rules, the political and ideational aspirations that underlie the regime. It is advocated that rather than being deserted, these aspirations should be revitalised. However, many recent proposals for the overhaul of the international tax regime point beyond the elements that have traditionally governed the interpretation of economic allegiance.[66] For instance, emphasising the value-creating role of digital services' users may shift the economic allegiance from the production jurisdiction towards the market jurisdiction.[67] The exceptions aside, a host of recent reform proposals have pleaded that an essential link between taxation and economic value creation must be identified.

The international tax regime, as developed for the purpose of allocating taxing rights horizontally among countries, exhibits several important properties. First, it acknowledged the normative significance of the reciprocal relationship between taxation and economy. This was obvious in the doctrines of economic allegiance and territorial taxation, which enforced the benefit aspects of taxation. In this regard, it must be borne in mind that the international tax regime related merely to income taxation. Thus, in the overall system of taxation and besides income taxation, consumption taxes remained in operation and were imposed on a basis of economic allegiance, which once again emphasised the benefit aspects of taxation. Second, taxing rights were not distributed solely with reference to territorial connections. The ability-to-pay principle, having gained political and academic traction, insisted on accommodating income taxes to the taxpayers' overall and worldwide socio-economic circumstances, which reflected taxpayers' actual ability to pay taxes. The international tax regime was thus shaped by the ability-to pay as well as benefit aspects of taxation. Third, the coexistence of benefit and ability-to-pay premises resulted in a tiered or layered structure of the tax regime. Drawing on benefit taxation, the power to tax was allocated to the source country, while on the basis of

[65] For instance, see Dietsch and Rixen (n 47).

[66] See W Haslehner and M Lamensch, 'General Report on Value Creation and Taxation: Outlining the Debate' in W Haslehner and M Lamensch (eds), *Taxation and Value Creation* (IBFD 2021).

[67] J Hey, '"Taxation Where Value is Created" and the OECD/G20 Base Erosion and Profit Shifting Initiative' (2018) 72 *Bulletin for International Taxation* 203; J Becker and J Englisch, 'Taxing Where Value is Created: What's "User Involvement" Got to Do with It?' (2019) 47 *Intertax* 161; W Schön, 'One Answer to Why and How to Tax the Digitalized Economy' (2019) 47 *Intertax* 1003.

ability-to-pay taxation, it was assigned to the taxpayer's country of residence. Source country taxation respected territoriality and economic allegiance, and it was legitimised by ideas that had traditionally justified the exercise of the power to tax in a vertical relationship between state and individual. Country of residence taxation was also legitimised with respect to economic allegiance. Beyond that, however, taxation by the country of residence was founded on the capacity of the country of residence to enforce ability-to-pay taxation and generate tax fairness in a horizontal relationship between taxpayers. Thus, in the dual system of an international tax regime, separate political entities were allowed to assert their taxing rights under partly different premises. The source country makes a claim on the basis of the territorial connection between taxation and economy, while the country of residence also resorts to considerations pertaining to inter-individual tax fairness and social justice.

IV. THE EU AS A SECOND-ORDER SYSTEM OF ENABLING ECONOMIC VALUE FORMATION

In developing the international tax regime, the goal was the proper horizontal allocation of taxing powers among nation states. In the context of the EU, the issue transforms into the vertical allocation of taxing powers between the EU and its Member States. This vertical allocation of taxing powers differs from the interstate allocation in two related respects. First, in their horizontal relationship, states are politically autonomous governing units. In the multi-level European political structure, in contrast, there is a normative division of governing functions and competences between the EU and its Member States. The EU is thus legally and functionally intertwined with its Member States, and vice versa. Second, notwithstanding certain recent efforts regarding the determination of corporate tax bases[68] and even tax rates,[69] the horizontal allocation has not, so far, involved the positive construction of the power to collect taxes, as the key aspiration has been to avoid excessive tax burdens. The international tax regime prescribes the limits to the authority of states to tax but abstains from imposing on states any obligation to collect taxes.[70] In the EU, the problem is related to the positive construction of the EU's power to collect taxes. The power would be instrumental in enabling the functional allocation of governing

[68] Council Directive (EU) 1164/2016 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market [2016] OJ L193/1.

[69] European Commission, 'Proposal for a Council Directive on Ensuring a Global minimum level of Taxation for Multinational Groups in the Union' COM(2021) 823 final.

[70] J Jaakkola and R Knuutinen, 'The International Order of Corporate Taxation: From Market-Building to Sustainable Fiscal Settlement?' in B Sjåfjell and CM Bruner (eds), *The Cambridge Handbook of Corporate Law, Corporate Governance and Sustainability* (Cambridge University Press 2020).

duties between the EU and its Member States. These two differences aside, this section reflects on whether the international tax regime's traditional principles and structures, legitimising tax collection in national polities, are meaningful for a review of the legitimacy of the EU's power to levy taxes.

The international tax regime's key lesson for the European power to tax is its dual structure. In this structure, taxation by the source country is legitimised through its value-enabling capacity, and taxation by the country of residence is legitimised through both its value-enabling capacity as well as its ability to execute socio-economic equity among individuals. In the relationship between the EU and its Member States, the dual structure of taxation has never been in operation: since the early phase of integration, Member States have retained their power to collect taxes, and the EEC and its successors have been financed by means mainly other than taxes, regardless of contrary political pursuits.[71] This is striking, as the dual structure of the international tax regime bears a relevant resemblance to the original two-tiered model of European integration, which was authoritative beyond tax-collecting powers. In this model, European market integration was assumed to generate economic growth and aggregate wealth across borders, while Member States had the mandate to redistribute resources between individuals and implement democratically established standards for social justice.[72] In this two-tiered system, the 'integration process was meant to expand the size of the (economic) cake, and the Member States were meant to redistribute that cake internally'.[73] The system was part of the broader post-war settlement of 'embedded liberalism',[74] in which national welfare regimes and international market order coexisted and reinforced each other.

To confer the power to collect taxes on the EU would not hinder Member States' prospects of using taxes for their democratically established ends. Member States, as the primary sites of the European taxpayer's social and economic ties, would retain their power to tax alongside the EU, and they would still be allowed to use taxes for various fiscal and redistributive purposes. In this sense, Member States would be reminiscent of countries of residence, whose right to tax was based on their contribution to the economic process, their capacity to enforce socio-economic fairness, and their ability to do justice to the

[71] AJ Menéndez, 'Neumark Vindicated: the Three Patterns of Europeanisation of National Tax Systems and the Future of the Social and Democratic *Rechtsstaat*' in D Chalmers, M Jachtenfuchs and C Joerges (eds), *The End of the Eurocrats' Dream: Adjusting to European Diversity* (Cambridge University Press 2016) 80–87.

[72] AS Milward, *The European Rescue of the Nation-State* (Routledge 1992); C Joerges, 'The Rechtsstaat and Social Europe: How a Classical Tension Resurfaces in the European Integration Process' in L Morlino and G Palombella (eds), *Rule of Law and Democracy: Inquiries into Internal and External Issues* (Brill 2010).

[73] F de Witte, 'The Architecture of a "Social Market Economy"' in P Koutrakos and J Snell (eds), *Research Handbook on the Law of the EU's Internal Market* (Edward Elgar Publishing 2017) 117.

[74] JG Ruggie, 'International Regimes, Transactions, and Change: Embedded Liberalism in the Postwar Economic Order' (1982) 36 *International Organization* 379.

taxpayer's personal circumstances. Therefore, dismantling national power to tax is not a part of the agenda. The question, rather, is whether there are legitimate grounds to grant the EU the power to collect taxes alongside Member States. Or, more precisely, can the EU be claimed to play a relevant similar role to the one that national polities, in their source country capacity, play in enabling value creation? Provided that the EU, as a second-order polity, makes a conceivable contribution, alongside Member States as first-order polities, to value creation, it could make a claim to tax the value it enables. In fact, over the last 10 years or so, this has emerged as perhaps the chief path of legitimising the EU's power to collect taxes.

Over the past decade, the EU's productive contribution to the accrual of economic value has been increasingly conceptualised as a 'European added value', which amounts to 'the value resulting from an EU intervention which is additional to the value that would have been otherwise created by Member States acting alone'.[75] I submit that there are two key mechanisms for the generation of a European added value or European public goods. The first is the legislative creation of the European internal market. Ever since the inception of the European communities in the 1950s, the European market has been the primary means of contributing to economic growth. Originally, this was intimately linked to the idea of 'dynamic growth', which characterised then-contemporary economic theories and which the architects of the European market equated with economies of scale, improved conditions of private competition, and increased productivity of investments.[76] For these rewards to emerge, competition law and the cross-border economic freedoms were established through European law. As a result, the regional system of Europeanised market economy, as a primary site of economic value creation, was no longer sustained solely through national legal systems, but a significant part of the legal substructure enabling private value creation was shifted to the European level. The second typical mechanism for generating European added value is budgetary expenditure and investment-type spending in particular. This spending has usually been implemented through various funds, from which pooled resources are distributed and whose significance has increased during the course of integration.[77] Recently, investment-type spending reached notable importance and topicality as the NextGenerationEU recovery instrument was adopted. The more these funds benefit the whole of the EU and the more they hold a genuinely European added value, the less they are bound to appear as an object of a *juste retour* zero-sum game in political bargaining.[78]

[75] European Commission, 'The Added Value of the EU budget' Commission Staff Working Paper SEC(2011) 867 final, 2.

[76] C Kaupa, *The Pluralist Character of the European Economic Constitution* (Hart Publishing 2016) 36–45.

[77] D Hodson, 'Regional and Structural Funds' in E Jones, A Menon and S Weatherill (eds), *The Oxford Handbook of the European Union* (Oxford University Press 2012).

[78] M Monti et al, 'Future financing of the EU: Final Report and Recommendations of the High Level Group on Own Resources' (December 2016) 30.

Drawing on the premise of benefit taxation, the European added value provides a basis for a European power to collect taxes. EU policies are contributory causes in the process of value creation, and the value not accrued in the absence of such policies may be taxed by the Union. This is most obvious with respect to the internal market, but the case can be made regarding public investments as well.[79] In line with the benefit theory, albeit routinely without reference thereto, it has been suggested that the focus of EU taxes 'should be on fresh receipts from activities immediately linked to the process of Europeanisation and globalisation', and that taxing this activity 'could quite reasonably and even profitably be mobilised to pay for the collective action that is its necessary concomitant and precondition'.[80] Without a doubt, the gains accruing in the internal market cannot be attributed entirely to the EU. Rather, the EU and Member States have a co-original effect in contributing to the existence of economic activity and the value it entails. This co-originality is familiar from the double tax context. In allocating taxing rights with deference to economic allegiance, it may be hard to determine the true and exclusive origin of specific activities. The right to tax dividend income, for instance, may be attributed to both source countries and countries of residence, as both may be seen to play a role in its formation. Likewise, in the European two-tiered system of economy, the public framework that enables market activities cannot be exclusively reduced either to its European or national pillar. This requires that the legal aspects of value creation are taken seriously. The EU does not come with its own population and it does entail a territorial extension, in a tangible and material sense. However, through its legal substructure and resource system, the EU contributes to value formation in an intangible way characteristic to the second-order and post-national systems of governance.

In allocating tax bases under the EU's taxing authority, the cross-border element of economic activities is a key, for two reasons. First, cross-border activities are a prototypical instance of the type of 'economic activity enabled by the internal market', and hence, they are linked to the European enabling policies and taxing authority.[81] From the benefit perspective, they are a legitimate target of taxation. Second, as a result of fiscal interdependence and tax competition, Member States' effective capacity to tax mobile tax bases within the internal market has diminished. Rather than being exogenous to the EU, this outcome can be traced back to the European market-making integration.[82] The internal

[79] G della Cananea, 'No Representation without Taxation in the European Union' in I Pernice and J Weiler (eds), *Legitimacy Issues of the European Union in the Face of Crisis* (Nomos 2017).

[80] D Tarschys, 'Entering a World of Footloose Tax Bases: Can the EU Generate Its Own Income?' in A de Feo and B Laffan (eds), *EU Own Resources: Momentum for a Reform?* (European University Institute 2016) 14.

[81] M Poiares Maduro, 'A New Governance for the European Union and the Euro: Democracy and Justice' (2012) RSCAS Policy Paper 11, 13.

[82] J Jaakkola, 'Enhancing Political Representation Through the European Economic Constitution? Regressive Politics of Democratic Inclusion' (2019) 15 *European Constitutional Law Review* 194.

market has thus facilitated an asymmetry between its benefits for private actors in their role as cross-border market citizens and disadvantages for governments in their role as tax collectors. However, the EU itself would be well positioned to tap mobile capital flows with a cross-border dimension, and it could 'aim for tax bases that are, more or less, beyond reach of individual states and accessible only by joint action'.[83] This would incorporate a corrective and balancing component into the European tax.[84] In essence, it would help Member States to adopt tax policies that are difficult to introduce and enforce under competitive pressures, prompted by transnational economic order. Addressing the negative fiscal externalities of integration would not interfere with the mandate of Member States to enforce their democratic conceptions of socio-economic fairness, but would rather compensate the losses incurred from the very process of integration. Therefore, in imposing taxes, the EU would act according to its perhaps primary functional role as an entity that solves collective action problems, and precisely in the field in which Member States have lost vital capacities to enforce their public policies.[85] In all this, the cross-border aspect and the taxpayer's degree of cross-border mobility would count as key factors in triggering the EU's legitimate power to collect taxes, and a European tax would relate to both positive and negative effects that the EU legal order entails.

Taxing cross-border activities by the EU would not merely generate revenues and limit fiscal externalities originating in the European market order. It could also alleviate Member States' struggles over the horizontal allocation of cross-border and mobile tax bases. In many cases, it appears notoriously hard to identify which Member State ought to be entitled to tax specific activities, as the territorial and value-enabling basis of taxation leaves much margin for interpretation. As stated in section III, the recent tax policy initiatives in the EU have widely endorsed the dogma of taxing where value is created. Implementing the principle in practice, however, has proven complicated, especially with respect to highly immaterial and mobile corporate activities. The EU's original common consolidated corporate tax base initiative of 2011, for instance, encountered fierce resistance because of the consolidation formula, according to which income was to be allocated between Member States.[86] Likewise, reinterpreting the concept of permanent establishment so that it would allow taxation of income (or revenue) from digital services in what is considered a proper site of economic activity has stalled.[87] Each time the reallocation of tax bases among

[83] Tarschys (n 80) 17. See also M Kumm, 'Democratic Challenges Arising from the Eurocrisis: What Kind of a Constitutional Crisis is Europe in and What Should Be Done about It?' in *Challenges of Multi-Tier Governance in the European Union: Effectiveness, Efficiency and Legitimacy* (European Parliament, 2013).

[84] Menéndez, 'Taxing Europe' (n 6) 324–25.

[85] Poiares Maduro (n 81) 11–16.

[86] For this, see European Commission, 'Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB)' COM(2016) 683 final.

[87] European Commission, 'Proposal for a Council Directive laying down rules relating to the corporate taxation of a significant digital presence' COM(2018) 147 final.

Member States is pursued by political means, obstacles emerge. In these cases, a European tax might be a part of the solution.[88] Rather than struggling to opt for one country or another, the proper site of taxation and also value creation might be the European level. This would not merely be a forced compromise in a situation where no other feasible solution appears in sight. On the contrary, in the complex value-enabling fabric of the European polity, the European level might well be the appropriate site of value creation, especially for cross-border activities.

Underlining the internal market benefits as a ground for instituting tax obligations often results in the conclusion that cross-border corporate entities and mobile financial capital ought to bear the tax burden, and correctly so. Yet, at the same time, European taxes are also portrayed as a conceivable means of fostering individuals' democratic citizenship and participation in the EU polity. Taxes could enhance European citizens' sense of political belonging in the EU, make the functioning of the EU system of governance more transparent to the citizens, raise their awareness of how the EU machinery functions, and increase their attentiveness to European politics.[89] To put it simply, European taxes would have a democratically productive role in reinforcing the link between individuals and the EU. This perception is affiliated with the broad strand of scholarship discussing the constructive role of taxation in building the modern state, nation and democratic institutions.[90] In the context of the EU, authors often stress that taxation would make the financial burden that the European polity imposes on individuals visible and transparent. However, on a more fundamental level, paying taxes is a key form of belonging to a political community and engendering a sense of authorship over the polity in which people's lives are essentially formed and through which individuals connect to each other's fate.

The two lines of reasoning above – the one considering mobile economic actors as an exclusive group of European taxpayers, the other stressing taxes as an essential means for a sense of political belonging – are difficult to accommodate simultaneously. If EU tax liabilities are merely allocated to cross-border corporate actors and financial capital, the European taxes are bound to remain distant to a great number of European citizens, and the broad-based financial

[88] See I Begg, 'The Challenges of Multi-Tier Governance in the EU: Budgetary Solidarity in a Multi-Tiered Union' in *Challenges of Multi-Tier Governance in the European Union: Effectiveness, Efficiency and Legitimacy* (European Parliament, 2013) 185.

[89] See Menéndez, 'Taxing Europe' (n 6); Le Cacheux (n 7); S Osterloh, F Heinemann and P Mohl, 'The EU Tax Revisited: Should There Be One? And Will There Be One?' (2008) 6 *Zeitschrift für Staats- und Europawissenschaften (ZSE) / Journal for Comparative Government and European Policy* 444, 449–51.

[90] For a discussion in different contexts, see RH Bates and D-HD Lien, 'A Note on Taxation, Development, and Representative Government' (1985) 14 *Politics & Society* 53; C Tilly, *Coercion, Capital and European States AD 990–1992* (Blackwell 1994); M Herb, 'Taxation and Representation' (2003) 38 *Studies in Comparative International Development* 3; ML Ross, 'Does Taxation Lead to Representation?' (2004) 34 *British Journal of Political Science* 229.

commitment to a polity, as a democracy-enhancing obligation, would still be missing. In fact, excluding European citizens from the body of taxpayers might facilitate the image of the EU as a community of capital and corporations, alienating citizens from the EU as a polity far from their own making. Therefore, if we consider fiscal obligations as essential components of democratic citizenship, associating the internal market benefits solely with corporations and financial capital might be counterproductive. Reducing the addressees of internal market benefits exclusively to corporate actors and finance might also disregard the fact that the internal market is not unconnected to European citizens, as citizens also have relevant economic ties to the European market. Furthermore, benefits from European investment-type expenditure are not confined to the corporate sector, of which the NextGenerationEU recovery package is a recent and in all likelihood not the last but rather an inaugural example. European citizens have relevant economic connections to the EU, and these are capable of justifying tax obligations beyond the business sector and providing for the political agency through citizen obligations. Therefore, an inclusive conception of European taxpayers would not entail that the link between the right to levy taxes and participation in the economy, as a basis for fiscal obligations, be abandoned. Indeed, the precise allocation of the tax burden between different groups of taxpayers is a topic that cannot be avoided in the EU context in the long run.

The fundamental question of who ought to be in the taxpayer position has been partly settled in the national context for quite some time, as national laws have embraced a broad taxpayer base. However, in the second-order polity of the EU, in which genuine tax obligations are still waiting to be introduced, the issue remains critical. I have proposed that the EU's contribution to the economic value formation provides a strong normative case for genuine EU taxes. The creation of these European taxes could involve pertinent reflections on various types of connections that exist between economy, taxation and individuals. Therefore, while the efforts of engineering EU taxes may rely on traditional tax policy principles, they may also entail a meaningful reinterpretation and rearticulation of those essentials. Future quarrels over the EU's revenue structure could thus make a significant contribution to tax-theoretical ideas, usually rather resistant to historical change.

V. CONCLUSION

In this chapter, the idea of systemic and functional reciprocity between taxation and economy has been treated as legitimising taxation in national, international and EU contexts. The chapter has put forward that in each setting, the power to collect taxes enables economic value creation, which justifies imposing taxes on the value being accrued. This pattern of thought has made an influential appearance through modern fiscal history and profoundly shaped the political rule. The chapter has also suggested that the EU's power to levy taxes, a capacity thus far non-existent in any significant sense, could be legitimised on such a

basis. Although an admittedly unconventional polity, the EU's power to collect taxes may nonetheless be justified with reference to the powerful ideas developed in national and international contexts. In this view, the EU is considered a second-order value-enabling entity, whose power to collect taxes would match the already existing functions the EU plays in the European multi-level political structure. Rather than a revolutionary act, the conferral of tax-collecting power on the EU would signify a coherent step in the European integration process. In terms of institutional design, moving on from mere governance of national tax systems to governing through genuine European taxes would signify a considerable change. From a long-term historical and ideational perspective, however, even liberal political systems with limited government have allowed states to collect taxes to finance their governing functions. Therefore, rather than deeply ideational, the change would be real-political.

This chapter has asserted that the EU has a legitimate claim to tax the value it enables. In the nation-state context, the same argument has typically been employed to legitimise a very specific task of taxation, namely the fiscal function of raising revenues. This has also been the case in the present chapter, which has only reflected on the revenue-raising function of taxes at the EU level. In no way, however, has this approach been intended to constrain the use of taxation for various socio-economic purposes beyond collecting revenues. The starting point of the chapter has been the two-tiered structure of the European polity, in which the task of enforcing socio-economic fairness between individuals by means of taxation rests chiefly on the Member States. The EU, for its part, has its primary duty in providing genuinely European collective or public goods, which have an added value across borders and for the body of European citizens at large. The two-tiered division of labour, however, is not a fixed given. Should the EU adopt an orientation towards a more redistributive community, European taxes could well be designed according to these preferences and reviewed against further legitimising principles. In the contemporary Union, in which the almost total absence of European power to levy taxes prevails, legitimising such a power must start from a relatively moderate premise. In this sense, the value-enabling role of the EU is not a restrictive and exclusive premise for justifying European taxes. It rather shows how imperfectly the current revenue system of the Union corresponds even to the liberal conception of the polity and the confined role that taxes are expected to play therein.

The Eurozone and Covid-19 crises have provoked lively political debates on the finances and revenues of the EU. Since the European Commission has prepared to deliver proposals on the new sources of EU resources, and since these will include different forms of taxation too, 'the next phase of implementing the own resources roadmap will inevitably involve the discussion of new or harmonised forms of taxation'.[91] In this exchange of views, the proposals must be reviewed against the proper and sustainable grounds of justification.

[91] R Crowe, 'An EU Budget of States and Citizens' (2020) 26 *European Law Journal* 331, 342.

Furthermore, whatever the eventual response at the European level, it must naturally comply with the dictum of 'no taxation without representation', ie, it must come with democratic legitimacy. However, it has been pointed out that just as there cannot be taxation without representation, there cannot be representation without taxation.[92] The European Parliament that has some say over spending but lacks the power to decide on taxes covering that spending is a structurally bounded representative body. It is true that enhancing the power to tax is by no means a guarantee for a democratic organisation. Nonetheless, with this caveat in mind, European taxes could enhance the governing capacities at the European level and forge representative structures. In the end, a direct allegiance between the EU and the European individual in the role of a taxpayer could perhaps foster democratic agency in the polity that is in danger of remaining politically distant and opaque. The European connection between taxation and democracy might thus prove reciprocal and symbiotic.

[92] S Fabbrini, 'Representation Without Taxation: An Association or Union of States?' in A de Feo and B Laffan (eds), *EU Own Resources: Momentum for a Reform?* (European University Institute 2016); della Cananea (n 79).