JUDGMENT OF THE COURT
10 MARCH 1970[1]

Commission of the European Communities v Government of the Italian Republic[2]

Case 7/69

Summary

Obligations of Member States — Failure to fulfil — Application by the Commission — Subject-matter — Alteration in the course of the proceedings — Inadmissibility
(EEC Treaty, Article 169)

Because of the importance which the Treaty attaches to the action available to the Community against Member States for failure to fulfil obligations, this procedure is in Article 169 surrounded by guarantees which must not be ignored, particularly in view of the obligation imposed by Article 171 on Member States to take as a consequence of this action the necessary measures to comply with the judgment of the Court. Accordingly the Court cannot give judgment on a failure to fulfil an obligation occurring after legislation has been amended during the course of the proceedings without thereby adversely affecting the rights of the Member State to put forward its arguments in defence based on complaints formulated according to the procedure laid down by Article 169. In such circumstances it is for the Commission to commence new proceedings under Article 169 with regard to the effects of the legislation, and if necessary to refer to the Court the specific shortcoming upon which it desires the Court to pronounce.

In Case 7/69

COMMISSION OF THE EUROPEAN COMMUNITIES, represented by Giuseppe Marchesini, acting as Agent, with an address for service in Luxembourg at the Chambers of Émile Reuter, 4, boulevard Royal,

applicant,

v

GOVERNMENT OF THE ITALIAN REPUBLIC, represented by Adolfo Maresca, Minister Plenipotentiary, acting as Agent, assisted by Pietro Peronaci, Deputy State Advocate-General, with an address for service in Luxembourg at the Italian Embassy,

defendant,

1 — Language of the Case: Italian.
2 — CMLR.

Application for a declaration that the Italian Republic, by applying a system of turnover tax which places a heavier burden on skin wool and carded or combed wool imported from other Member States of the EEC than on similar domestic products, has failed to fufil the obligation placed on it by Article 95 of the Treaty establishing the European Economic Community,

THE COURT

composed of: R. Lecourt, President, R. Monaco and P. Pescatore, Presidents of Chambers, A. M. Donner (Rapporteur), A. Trabucchi, W. Strauß and J. Mertens de Wilmars, Judges,

Advocate General: K. Roemer
Registrar: A. Van Houtte

gives the following

JUDGMENT

Issues of fact and of law

I — Facts and procedure

The facts and procedure in this case may be summarized as follows:
Proceedings under Article 169 of the Treaty were initiated by the (then) Commission of the European Economic Community by a letter of 12 July 1966 against the Italian Republic, on the ground that it had infringed Articles 95 and 96 of the EEC Treaty by the manner in which it applied its 'imposta generale sull'entrata,' (general turnover tax) the additional rate thereon, and the 'imposta di conguaglio' (equalization tax) to all the products.
Subsequent discussions largely disposed of the infringements complained of but the Commission considered that certain contraventions of Article 95, to which it referred in its letter of 12 July 1966, continued to exist and it therefore delivered a reasoned opinion on the matter to the Italian Republic on 16 July 1968.

Since the Italian Republic did not comply with the reasoned opinion within the period laid down, the Commission brought the matter before the Court by means of the present application which was lodged at the Registry on 4 February 1969.
The alleged contraventions were described in the reasoned opinion as follows:

'(a) The "imposta generale sull'entrata" (IGE) applicable to imported wool obtained by the dewoolling of skins

Skins intended to be used for the production of wool by dewoolling, whether local or imported, are subject to the IGE at a rate of 2.4%. On completion of dewoolling, the resultant wool is subject to an additional rate of 4%. The result of this system of taxation is that wool obtained in Italy by dewoolling skins bears a charge at a maximum rate of 6.4% (2.4% on skins+4% in addition on the wool). Only in one case,

where the national producer who has done the dewoolling sells the wool thus obtained, do the tax authorities apply the IGE at the basis rate of 7.2%, plus the additional rate of 4%. That is an extremely rare case, however, since the Italian industry is unusually well integrated, to such an extent that the dewoolling and subsequent operations are carried out by the same producer.
Skin wool imported from abroad, however, is subject to the IGE at the rate of 7.2% plus the additional 4%. In other words, the total tax which it bears is always 11.2% and that is far higher than that ordinarily borne by similar domestic products.

(b) The "imposta generale sull'entrata" on sheep's or lamb's wool, whether or not carded or combed

Wool in the above categories is subject to a comprehensive tax levied once and for all at the rate of 11.2%.
Whilst there is only one tax, however, the taxable value varies according to whether the products are domestic or imported.
In the former case, the rate is applied on each occasion to the value of the bulk wool, irrespective of whether it is in fact such, or has been carded or combed. In the second case however the rate is applied to the value at the time of importation. Thus for imported wool that is carded and combed, the tax is calculated on the basis of its actual value, whilst for similar domestic products this tax is payable on the value of the raw wool, which is obviously less.
These facts, and those described at (a) above constitute an infringement of Article 95 of the Treaty of Rome which forbids Member States to impose on the products of other Member States any internal taxation in excess of that imposed on similar domestic products.'
In a statement dated 15 July 1969 the defendant indicated that it had adopted on 2 July 1969 Decree-Law No 319, Articles 7 and 8 of which provide in particular for:

(a) payment of the IGE at the rate of 2.5% on wool obtained by dewoolling of skins when it passes from the dewoolling shop to the processing works;

(b) a reduction of 3.6% on the special additional tax provided for by Decree-Law No 1118 of 7 October 1965 and in its subsequent amendments and extensions, and applicable to new materials of wool destined to become carded and combed wool; account is taken (as regards the greasy wool referred to by the Commission in its comparison) of the fact that it is subsequently chargeable with the IGE at the rate of 2.8% on the cost of the carding and combing processes.
It considered that in view of this the necessary requirements for the Commission to withdraw its application could be met.
In a letter of 4 August 1969 the applicant stated that in its opinion the facts set out in the statement were not sufficient to show that the infringement against Article 95 had been completely eliminated and, as a result, it was continuing the proceedings.
The written procedure followed the normal course.
After hearing the report of the Judge-Rapporteur and the views of the Advocate-General the Court decided to open the oral procedure without any preparatory inquiry.
The parties presented oral argument at the hearing on 26 November 1969.
The Advocate-General delivered his opinion at the hearing on 20 January 1970.

II — Conclusions of the parties

The *applicant* claims that the Court should:

— declare that the Italian Republic has failed to fulfil the obligation imposed on it by Article 95 of the Treaty establishing the EEC by applying a system of turnover tax which levies on imported skin wool and imported carded or combed wool from other Member States of the EEC a higher rate than on similar domestic products;

— order the defendant to pay the costs.

The *defendant* contends that the Court should:

— dismiss the application by the Commis-

sion of the European Communities;

— order the Commission to pay the costs.

III — Submissions and arguments of the parties

The submissions and arguments of the parties may be summarized as follows:

A — *Admissibility of the application*

The *applicant* considers its application to be admissible.

The *defendant* did not contest this in its pleadings.

However, in the course of the oral procedure the defendant claimed that as a result of amendments made to the Italian fiscal law by Decree-Law No 319 of 2 July 1969 the application has lost its purpose and must therefore be declared inadmissible.

The *applicant* replied by claiming that on the one hand the modifications made did not eliminate all infringements of the provisions of the Treaty and that on the other hand even if this were so it was desirable that the Court should declare that prior to 2 July 1969 the Italian Republic failed to fulfil its obligations.

B — *The substance of the case*

(a) Infringement of Article 95 by reason of the fact that the turnover tax levied on imported wool obtained by the dewoolling of skins was in excess of that on similar domestic products

The *applicant* describes the system of taxation introduced by the Italian Law No 757 of 12 August 1957, as subsequently amended and supplemented.

Despite the apparent similarity between the system applicable to domestic wool and the one applicable to imported wool, examination of the actual position reveals a serious discrimination. The sale of wool to another manufacturer by a national producer who has carried out the dewoolling, a sale subject to turnover tax at a rate of 7.20%, is in fact an extremely rare case. The Italian industry is very well integrated in this sector, inasmuch as—in virtually every case—the skins are dewoolled and the wool thus obtained is subsequently processed by a single manufacturer.

Consequently domestic wool obtained by dewoolling skins is not generally liable to the tax of 7.2% but only to the supplement of 4%. On the other hand, imported skin wool is in every case subject to payment of both the rate of 7.2% and the special supplement of 4%. As a result it is subject to the turnover tax at a higher rate than that payable on domestic wool, and this constitutes a failure to fulfil the obligation not to impose directly or indirectly any taxation on products of other Member States in excess of that imposed on similar domestic products.

The *defendant* considers the Commission's observations not pertinent to the issue.

The Treaty does not lay down the principle that a producer, once he has reached a certain point in the industrial process, must sell the semi-finished product to someone else, since there is an inflow of Community imports at the later processing stage. The principle laid down by Article 95 is that the internal taxation imposed by a Member State on the products of another Member State must not be in excess of that applicable to similar domestic products.

This principle has been strictly observed in the present case since, as the Commission itself acknowledges, the rates of tax are the same irrespective of whether the products concerned are domestic or come from Member States, and therefore the allegation of an infringement of Article 95 of the Treaty is quite unfounded.

Furthermore the Commission has not taken into account the fact that the manufacturer who undertakes both the dewoolling and the subsequent treatment of the wool incurs in the course of the whole cycle all the costs of processing, including those relating to the depreciation of machinery and, more significantly, losses arising during processing.

In its reply the *applicant* repeats that whilst the conditions in which the tax applies are always present in the case of imported wool

they are never or almost never all present in the case of similar domestic wools. Article 2 (a) of Law No 757 of 12 August 1957 stipulates that the turnover tax shall apply 'to domestic products when sold by the producer and, in the case of products which have to be placed in stock, when sold by the stockers.' The sale of semi-finished products is thus a rare occurrence in the case of domestic products in this sector.

The anomaly of the special treatment reserved in practice for domestic wool is confirmed by a comparison with the last paragraph of Article 3 of Decree-Law No 1118 of 7 October 1965 as it stands after subsequent amendments, which provides that 'undertakings which carry out the dewoolling of skins at their own places of business or those of third parties..., shall be obliged to pay the special supplement of 4%... on the wholesale price of the wool, *at the time of sale of the product or at the time when this passes from the dewoolling section to the section where it is to be processed.*'

The result is that domestic wool which passes on to the final processing stage within the undertaking which has already done the dewoolling is subject to the special supplement without ever having been subject to the turnover tax at the basic rate.

All the above points to Article 2 (a) of Law No 757 of 12 August 1957 as being the origin of the discrimination complained of inasmuch as it limits to one instance only (sale) the application of the basic rate of tax on domestic wool.

After producing a table of the practical results of the application of the Italian legislation in question, the applicant replies to the Italian Government's objection that the applicant did not take into account the costs incurred by the producer who carries out both dewoolling and subsequent processing, and claims that it is precisely the function of the equalization tax—a tax wholly distinct from that in question here—to compensate for those costs.

At the end of its reply the applicant, both with regard to the present complaint and the following one, contests the conclusions of the defendant in which it is claimed that the situation complained of is merely the natural result of the special structure of the Italian wool industry or of the actions of the heads of undertakings, who cannot be coerced, and so cannot amount to an infringement of Article 95 of the Treaty. The difference in treatment complained of lies, it states, in the advantages with regard to taxation enjoyed exclusively by the Italian producers and made possible by express legal provisions.

The *defendant* contends in its rejoinder that if the practical consequences of the application of the provisions in question are considered it will be seen that the rate of 11.2% borne by imported wool is in fact lower than the tax on domestic products (12.24%). This is explained, in particular, by the fact that whilst the tax of 2.4% is calculated on the basis of skins with the wool still on them the tax is in fact eventually charged at the rate of 5.74% on wool on the back.

In the course of the oral procedure the defendant remarked that when the IGE is charged on the sale of wool obtained by the dewoolling of skins by the producer who carried this out it is intended to apply to any sale between different legal or natural persons. It follows that the transfer from one legal person to another of wool obtained by dewoolling is chargeable with the IGE even where those legal persons are parts of a single economic unit.

(b) Infringement of Article 95 by reason of the turnover tax levied on imported carded and combed wool being in excess of that on similar national products

The *applicant* explains that according to the last paragraph of Article 2 of Law No 757 of 12 August 1957, as far as these products are concerned, the turnover tax paid in the course of processing 'absorbs' that chargeable on the turnover of the products obtained at the end of the processing. As a result all tax liability in respect of domestic carded or combed wool could have been discharged once and for all at the time of sale (as regards sheared wool) or at the time when it passed to later stages in the processing cycle (skin wool), when such wool was still not combed or carded, so that it has an advantage by reason of the lower chargeable value for tax purposes constituted by wool which is not combed or carded.

Conversely, carded or combed wool coming from abroad, including Member States of the Community, is subject to tax on the actual, and higher, value which it constitutes in this state when it is imported.
All carded or combed wool which is imported is therefore at a disadvantage by reason of the fact that the chargeable value for tax purposes is different from that which applies to the similar domestic products. Such a situation amounts to a further infringement of Article 95 of the Treaty.
The *defendant* considers that this claim is equally devoid of foundation because the wool is taxed at the same rate and because it is quite normal in practice for the amount of tax on the product having the higher value to be greater than the amount of tax on the product having the lower value.
On the other hand wool sold in the raw state, coming from abroad, is subject to the same tax as that produced in Italy.
The equal treatment with regard to tax laid down by Article 95 of the Treaty concerns similar products and a comparison between two different products such as raw wool, on one hand, and carded or combed wool, on the other hand, is not therefore relevant.
In the reply the *applicant* claims that the tax advantage constituted by the 'absorption' system is virtually unobtainable for wool which has already been carded or combed and coming from other Member States, since the basic rate and the supplementary charges apply solely to the value at the time of importation. The difference in the chargeable value for tax purposes in the two cases (domestic products and imported products) could be as much as 20%.
The Commission observes further that the discrimination complained of under the present sub-heading also applies to wool which is not combed or carded obtained by dewoolling skins, so that it almost always becomes an additional discrimination to the one complained of under subheading (a).
In the rejoinder the *defendant* repeats its submissions, declaring in particular that the action brought by the Commission has been deprived of any foundation as a result of the amendments recently made to the Italian legislation in question.

Grounds of judgment

1 After issuing its reasoned opinion of 17 July 1968 the Commission, in an application lodged on 4 February 1969, requested the Court under Article 169 of the EEC Treaty 'to declare that the Italian Republic, by applying a system of turnover tax which places a heavier burden on skin wool and carded or combed wool imported from other Member States of the EEC than on similar domestic products, has failed to fulfil the obligation placed on it by Article 95 of the Treaty'.

2 In a written statement submitted on 26 July 1969 the Italian Republic observed that a Decree-Law of 2 July 1969, which amended the tax system in dispute was, in its opinion, of such a nature as to call for the withdrawal of the application. The Commission replied that the provisions of this Decree-Law did not make it possible to draw the conclusion that in the present case any infringement of Article 95 of the Treaty had ceased and that consequently it could not consider any course of action other than to continue with the case.

3 However, the parties have devoted since then the major part of their arguments to the effects and the burden of the tax system brought into operation by the said Decree-Law. The Commission does not, moreover, refer to any objective other than that of putting an effective end to the specific violation alleged against the Italian Republic, so that its only aim appears to be to terminate any violation which may still exist.

4 It follows from the foregoing that, although the parties still disagree about the effects of the above-mentioned Decree-Law, they have nevertheless taken the view that this measure substantially affects the outcome of the present dispute and they have accordingly requested the Court to consider the resulting situation as a whole. In so doing the applicant has thus amended the subject-matter of its application so that it is no longer concerned only with the question whether at the time when the application was lodged there was a failure on the part of the Italian Republic to fulfil its obligations under Article 95, but principally with the question whether this failure still continues after the coming into force of the Decree-Law.

5 In the present action it is not possible for the Court to decide whether the situation created by Decree-Law No 319 is compatible with the obligations imposed upon Member States under Article 95 of the Treaty. Because of the importance which the Treaty attaches to the action available to the Community against Member States for failure to fulfil obligations, this procedure in Article 169 is surrounded by guarantees which must not be ignored, particularly in view of the obligation imposed by Article 171 on Member States to take as a consequence of this action the necessary measures to comply with the judgment of the Court. Accordingly the Court cannot give judgment in the present case on the failure to fulfil an obligation occurring after legislation has been amended during the course of the proceedings without thereby adversely affecting the rights of the Member State to put forward its arguments in defence based on complaints formulated according to the procedure laid down by Article 169.

6 In such circumstances it is for the Commission to commence new proceedings under Article 169 with regard to the effects of Decree-Law No 319, and if necessary to refer to the Court the specific shortcoming upon which it desires the Court to pronounce. In view of the change in the subject-matter of the dispute, the request as originally formulated in the application must therefore be dismissed.

Costs

7 The reason for the dismissal of the application lies in the amendment of the Italian legislation and the consequent change in subject-matter of the application, as suggested by the defendant and accepted by the applicant.

This is an exceptional circumstance justifying application of the first subparagraph of Article 69 (3) of the Rules of Procedure. Therefore, the parties should be ordered to bear their own costs.

On those grounds,

Upon reading the pleadings;
Upon hearing the report of the Judge-Rapporteur;
Upon hearing the parties;
Upon hearing the opinion of the Advocate-General;
Having regard to the Treaty establishing the European Economic Community, especially Articles 95, 169 and 171;
Having regard to the Protocol on the Statute of the Court of Justice of the European Economic Community;
Having regard to the Rules of Procedure of the Court of Justice of the European Communities,

THE COURT

hereby:

1. **Dismisses the application;**

2. **Orders the parties to bear their own costs.**

Lecourt Monaco Pescatore

Donner Trabucchi Strauß Mertens de Wilmars

Delivered in open court in Luxembourg on 10 March 1970.

A. Van Houtte
Registrar

R. Lecourt
President

OPINION OF MR ADVOCATE-GENERAL ROEMER DELIVERED ON 20 JANUARY 1970[1]

Mr President,
Members of the Court,

On examining the Italian system of turnover tax, the Commission of the European Economic Community came to be convinced that some of the rules concerning the import of wool and wool products from other Member States infringed Articles 95 and 96 of the EEC Treaty. It therefore considered it necessary to initiate proceedings to establish these infringements of the

1 — Translated from the German.