OPINION OF MR ADVOCATE GENERAL CRUZ VILAÇA
delivered on 27 January 1988 *

Mr President,
Members of the Court,

1. The London Value-added Tax Tribunal has submitted to the Court of Justice, under Article 177 of the EEC Treaty, a number of questions for a preliminary ruling on the interpretation of Article 27 of the Sixth Council Directive (77/388/EEC) of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value-added tax: uniform basis of assessment, [1] and on the validity of a Council decision which, pursuant to that article, authorized the United Kingdom to adopt for two years a derogating measure to enable certain types of tax avoidance to be prevented. [2]

1. Background

2. The questions have been submitted in proceedings in which two United Kingdom companies — Direct Cosmetics Limited and Laughtons Photographs Limited — challenge the application of the aforesaid derogating measure to them. What is at issue, essentially, is the determination of the basis for charging value-added tax on the transactions of those companies, which, in view of their special nature, had led to the application of that measure.

3. These proceedings follow on from another case already decided by the Court, [3] which also involved one of the parties to these proceedings (Direct Cosmetics) and the Commissioners of Customs and Excise. That case was concerned with the question whether or not it was necessary to notify the Commission, under Article 27 (2) of the Sixth Directive, of an amendment to English tax legislation derogating from the basis of assessment defined in that directive.

4. In compliance with the judgment of the Court, which considered the aforesaid amendment to be a 'special measure' within the meaning of Article 27 (1) and therefore subject to authorization by the Council, the United Kingdom notified the Commission on 15 March 1985 of the scope of the measure which it was planning to introduce and which derogated from the Sixth Directive.

5. According to that notification, that derogation, whose validity was limited to a period of two years, was designed to combat tax avoidance by introducing a special system for charging value-added tax in cases in which the marketing structure of certain firms was based on the sale of their products to unregistered resellers.

6. In conformity with Article 27 (3), the Commission informed the other Member States of the request submitted. As no

* Translated from the Portuguese.

1 — Official Journal 1977 L 145, p. 1.

2 — Decision 85/369/EEC, with effect from 13 June 1985 (Official Journal 1985, L 199, p. 60).

3 — Judgment of 13 February 1985 in Case 5/84 *Direct Cosmetics* v *Commissioners of Customs and Excise* [1985] ECR 617.

request for the matter to be raised by the Council was made by any of the Member States or by the Commission itself within two months from the date on which the Member States were informed, the derogation was deemed to have been tacitly authorized as from 13 June 1985 in accordance with Article 27 (4).[4]

7. Following the grant of that authorization, paragraph 3 of Schedule 4 to the United Kingdom Value-added Tax 1983 provided as follows:

'Where —

(a) the whole or part of a business carried on by a taxable person consists in supplying to a number of persons goods to be sold whether by them or others, by retail, and

(b) those persons are not taxable persons, the Commissioners may by notice in writing to the taxable person direct that the value of any such supply by him after the giving of the notice or after such later date as may be specified in the notice shall be taken to be its open market value on a sale by retail.'

8. As regards the legislation previously in force (paragraph 2 of Schedule 3 to the Finance Act 1972, in its initial version), the amendment made thereto by paragraph 3 of Schedule 4 to the Value-added Tax Act 1983 consisted essentially in repealing the reference to a direction being necessary 'for the protection of the revenue'.

9. By directions of 25 June 1985 and 5 July 1985, whose wording (which is identical in both cases) need not be reproduced here, the Commissioners of Customs and Excise applied the aforesaid provision to the appellant companies.

10. The significance of those directions for their addressees is clear if the specific nature of their respective selling schemes is borne in mind. Those schemes are described in the Report for the Hearing and the scheme used by Direct Cosmetics Limited had already been referred to in the judgment of 13 February 1985.

11. I would merely recall that Direct Cosmetics Limited is a company specializing in direct sales of cosmetic products which cannot be sold on the ordinary retail market (surplus stocks, discontinued lines, products wrapped and packaged for Christmas but not sold in time for that occasion, and so on). Direct Cosmetics Limited buys those products directly from the manufacturers at reduced prices and then resells them in hospitals, factories and offices through agents who charge the company's catalogue price and pay over to the company the proceeds of sale. If the selling price is paid over within 14 days, the agent may retain a 20% discount, which constitutes his remuneration.

12. Laughtons Photographs Limited is a company which specializes in taking photographs of classes and individual children at school, the photographs being sold to the school in packages. The school subsequently resells the photographs to the children's

4 — Decision 85/369/EEC (Official Journal 1985, L 199, p. 60).

families, at a price which, according to the appellant company, may be equal to or higher than the price which the latter charges the school.

13. It is noteworthy that the agents through whom Direct Cosmetics Limited sells its products are not liable to value-added tax as their turnover is below the minimum laid down by United Kingdom legislation in accordance with Article 24 of the Sixth Directive. Similarly, schools are not liable to value-added tax on the photographs sold to them by Laughtons Photographs Limited and subsequently resold by them.

14. Those were the circumstances in which the two companies in question instituted proceedings before the London Value-added Tax Tribunal. They argued that the directions of the Commissioners of Customs and Excise were invalid as being outside the scope of the objectives referred to in Article 27 (1) of the Sixth Directive and those of the Council's authorizing decision of 31 July 1985. Moreover, they maintained that Article 11. A.1 (a) of the Sixth Directive was applicable on the ground that it had direct effect, and that, according to that provision, value-added tax was payable only on the consideration actually obtained by them.

15. Against that, the Commissioners of Customs and Excise argued that: (a) Article 11. A.1 (a) had been implemented in English law; (b) they had given proper notification of a special measure on the basis of a derogation validly authorized by the Council; and (c) the contested measure was an appropriate means of ensuring that tax was recoverable at the full value of the product at the retail stage.

2. The questions submitted for a preliminary ruling

16. The London Value-added Tax Tribunal stayed the proceedings and referred the following five questions to the Court of Justice for a preliminary ruling:

'1. Is a measure, such as that contained in paragraph 3, Schedule 4 of the Value-added Tax Act 1983, within the limits allowed by Article 27 (1) of the Sixth Directive, or is it wider than is strictly necessary?

2. Is such a measure which is applied to

(a) a taxpayer who has been accepted as carrying on business without any intention to evade or to avoid value-added tax and whose method of trading has evolved solely on account of commercial considerations,

(b) a taxpayer who has been accepted as carrying on business without any intention to evade or to avoid value-added tax and whose method of trading has evolved solely on account of commercial considerations but which may have the objective result that some tax has been avoided,

(c) some taxpayers but not against other such taxpayers who are selling directly to unregistered resellers

within the limits of the derogation allowed by Article 27 (1) of the Sixth Directive or is it wider than is strictly necessary?

3. Can such a measure be applied to taxpayers whose activities fall outside the matters referred to in Article 27 of the said Sixth Directive or outside the terms of the request for authorization or the terms of the actual authorization by the Council of Ministers?

4. Is the decision of authorization of the Council of Ministers invalid or of no effect for any substantive or procedural reason, such as the failure of the Council of Ministers or the Member States to evaluate or to be informed of the fact that the measure was not capable of being evaluated either against the criteria laid down in Article 27 of the Sixth Directive or against the principle of proportionality or against the basic principles of the Sixth Directive?

5. Does the decision of authorization of the Council of Ministers mean that an individual taxpayer, such as the appellant, who has been accepted as carrying on business without any intention to evade or to avoid value-added tax, cannot rely upon being taxed under the provisions laid down in Article 11. A.1 (a) of the Sixth Directive on value-added tax?'

17. It is necessary to rearrange the questions submitted, in so far as their wording is not conducive to the clarity required in the answers to be given.

18. The first two questions refer to the same general problem (the scope of the derogation provided for in Article 27 (1) of the Sixth Directive), the second one dealing in greater detail with certain aspects of the general problem raised in the first one.

19. As for the fifth question, it is closely connected with the examination of the first two questions, since the exclusion of Article 11. A.1 (a) is the result of the application of a validly authorized derogating measure.

20. *A* — In asking those questions, the national court seeks to ascertain essentially:

(1) whether Article 27 (1) of the Sixth Directive permits a special derogating measure to be applied in cases of objective tax avoidance in which no fraudulent intent on the part of the traders concerned is shown to exist;

(2) whether a special measure derogating from the Sixth Directive, such as paragraph 3 of Schedule 4 to the Value-added Tax Act 1983, falls within the scope of Article 27 (1) or whether it is disproportionate to the objective pursued thereby, namely the prevention of certain types of tax evasion or avoidance;

(3) whether Article 27 (1) is compatible with the application of the aforesaid measure only to some of the traders who sell directly to resellers who are not taxable persons;

(4) whether or not, in the light of the answers to be given to the previous questions, Article 11. A.1 (a) is to be declared inapplicable.

21. *B* — With regard to the first part of the third question, the answer follows inescapably, without any need for further explanations, from the answers to be given to the previous questions, if indeed the answer is not already contained in the very wording of the question. The second part of the third question is in fact concerned with the problem of the terms in which, under Article 27 (4), the Council can be regarded as having tacitly granted authorization for the adoption of the derogating measures.

22. The fourth question is again concerned with the problem of the conditions of validity of the Council's tacit authorizing decision. That is a problem which must be considered in connection with the other questions raised by the national court.

23. I propose to treat all the questions submitted as genuine problems concerning the interpretation of Article 27 and to deal with the answers to be given having regard to the fact that proceedings for a preliminary ruling are, in view of their specific nature, inappropriate for the purpose of interpreting national law and assessing its compatibility with Community law.

3. The general system of value-added tax

24. *A* — In order to answer those various questions, it is appropriate to begin by considering the Community's general system of value-added tax, as embodied in the Sixth Directive and its predecessors, in particular the First and Second Value-added Tax Directives.

25. *B* — As is well known, the latter two directives, both of 11 April 1967, laid down the basis for harmonizing national legislation concerning turnover taxes in the Member States of the Community.

26. The First Directive [5] made the adoption of value-added tax compulsory as from 1 January 1970 (later deferred to 1 January 1972) throughout the Community to replace the cumulative taxes that were previously applied in practically all the Member States (excluding France).

27. For its part, the Second Directive [6] laid down some of the — still rather flexible — general principles regulating the Community's system of value-added tax.

28. *C* — By comparison with cumulative taxes, the system of value-added tax presents a number of indisputable advantages. First and foremost, it is a *neutral* tax with regard to the fiscal treatment of both domestic and international transactions.

29. To begin with, value-added tax is a tax which does not interfere with the degree of industrial integration. The tax burden borne by goods is always the same, whatever the length of the production chain, inasmuch as it depends only on the value added at each stage, the taxes included in the price of intermediate goods and in the price of services being deductible at each stage (First

5 — Official Journal, English Special Edition 1967, p. 14.
6 — Official Journal, English Special Edition 1967, p. 16.

Directive, eighth recital in the preamble thereto and second paragraph of Article 2). The important point is that the sum of the value-added tax chargeable at every stage on the value added at each stage must be equal to the amount resulting from the application of a single-stage tax at the same rate chargeable only on the sale of goods by a retailer to the final consumer. Thus, value-added tax may be seen as 'a general tax on consumption exactly proportional to the price of the goods and services, whatever the number of transactions which take place in the production and distribution process before the stage at which tax is charged' (first paragraph of Article 2 of the First Directive).

30. Secondly, value-added tax permits tax adjustments to be made easily at the border by refunding to the exporter the taxes paid on inputs and by taxing imports in the country of destination at the rate applicable to domestic goods of the same kind. That ensures the abolition of discrimination between domestic and imported products and the removal of tax barriers to the free movement of goods within the Community, as long as it is not possible to abolish tax frontiers completely by the adoption of the so-called 'origins principle'.

31. If those are some of the fundamental objectives which the system of value-added tax is designed to achieve, it is clear that the tax must be applied as widely as possible since its effectiveness in relation to the objectives pursued increases in step with the size of the range of products and services to which it applies and with the number of transactions which it covers between the production stage and the retail stage. As is emphasized in the fifth recital in the preamble to the First Directive, 'a system of value-added tax achieves the highest degree of simplicity and of neutrality when the tax is levied in as general a manner as possible and when its scope covers all stages of production and distribution'.

32. In addition, the 'generalized application' of value-added tax is an essential element of its financial effectiveness, permitting a substantial revenue to be assured at standard rates of tax kept within reasonable limits (see the fourth recital in the preamble to the Second Directive).

33. *D* — The Sixth Directive marked a great leap forward in the achievement of the objectives of value-added tax at Community level, and gave significant impetus to the process of harmonizing taxation.

34. Both the First and the Second Directives, notwithstanding the fact that they laid down the basis for harmonizing national systems of indirect taxation, left open the possibility of numerous differences arising as regards the scope of the tax and introduced a very limited number of Community-law concepts.

35. The Sixth Directive, on the other hand, harmonized in all the Member States the basis for charging value-added tax, which led, by comparison with the Second Directive, to the widest possible application of the tax.

36. In the first place, the Sixth Directive imposed an obligation to include, in the taxable amount, the value added at the retail stage, which had previously been optional.

37. Secondly, the Sixth Directive imposed the tax on services and harmonized the list of exemptions which the Member States are authorized to grant.

38. It should be remembered, moreover, that the Sixth Directive pursued another immediate objective, namely the establishment of conditions enabling value-added tax to constitute a basis for calculating the Community's own resources. That made it essential to harmonize the basis of assessment, as a precondition for an equitable apportionment of the financial burdens between the various Member States.

39. *E* — However, the concern to charge VAT on the taxable amount in the most comprehensive manner on a general and uniform basis throughout the Community must contend with political and social imperatives involving the exclusion of certain transactions or certain categories of traders, with the weight of national fiscal habits and traditions, or with administrative difficulties and problems of economic organization, and with difficulties relating, in certain cases, to the rigorous identification and precise determination of the actual basis of assessment.

40. That is why, in the first place, the authors of the Sixth Directive were obliged to accept certain limits to the harmonization of the tax systems and provided for certain decisions to be optional (for instance Article 5 (5), (7) and (8), and Article 6 (3)) or left certain arrangements, either provisionally or definitively, to the discretion of the Member States or the taxable persons of those States (for instance Article 13C, the special scheme for small undertakings provided for in Article 24, the special schemes for farmers provided for in Article 25 and the transitional provisions of Article 28).

41. In addition, the directive laid down a common system of exemptions in Articles 13 to 16. However, in practice those exemptions apply essentially to certain types of transactions that are very difficult or impossible to include in the basis of assessment and to a series of expenses whose exemption is justified on weighty grounds of social policy.

42. Hence the directive went as far as it could with regard to the determination of the taxable amount, and, conversely, provided for the smallest possible number of exemptions to the principle of the general applicability of the tax.

43. That provides justification for not giving those exceptions a broad interpretation but rather, in so far as they run counter to the general rule, for giving them a strict interpretation.

44. Moreover, the Sixth Directive permitted the adoption of certain machinery designed to deal with situations which are particularly complex or which involve a risk of tax avoidance enabling part of the taxable amount to escape taxation.

45. Thus, the second subparagraph of Article 4 (4), widening the definition of taxable person in Article 4 (1), permits the Member States to treat 'as a single taxable person persons established in the territory of the country who, while legally independent, are closely bound to one another by financial, economic and organizational links'.

46. Article 27 (1), with the same end in view, provides that 'the Council, acting unanimously on a proposal from the Commission, may authorize any Member

State to introduce special measures for derogation from the provisions of this directive, in order to simplify the procedure for charging the tax or to prevent certain types of tax evasion or avoidance'.

47. In view of the wording of that provision, the possibility cannot be ruled out that the scope of the derogating measures may encompass Article 11, in particular Article 11. A.1 (a), which lays down the principle that, in every transaction (involving the supply of goods or the provision of services) the basis of assessment normally consists of the consideration which has been or is to be obtained by the supplier or by the person providing the services.

48. It is clear, however, that the legislature wished the measures adopted on the basis of Article 27 to depart as little as possible from the approach taken in the basic regulations. For that reason, it made a point of stating (second sentence of Article 27 (1)) that 'measures intended to simplify the procedure for charging the tax, except to a negligible extent, may not affect the amount of tax due at the final consumption stage'.

49. Similarly, the permissibility of special measures 'to prevent certain types of tax evasion or avoidance' must be taken to constitute a derogation which is not intended to run counter to the reasoning behind the Sixth Directive but aims instead at achieving its objectives as fully as possible.

50. The point is, basically, that, in the face of the difficulties raised by certain specific situations, provision must be made for the adoption of machinery capable of 'pursuing' the taxable amount and preventing, in view of the special circumstances in which the transactions in question are concluded, a part of it from escaping taxation and possibly giving rise to distortions (not necessarily resulting from 'unfair competition') in the fiscal treatment of situations which are, in economic or commercial terms, substantially identical.

51. In that case, as in the case of measures intended to simplify the procedure for charging the tax, the measures adopted may take various forms.[7] One of those forms is undoubtedly that which was used by the United Kingdom in paragraph 3 of Schedule 4 to the Value-added Tax Act 1983 and which was applied to the appellant companies.

52. It remains to be determined whether that form is lawful and whether it has been correctly applied.

53. I believe that the principles described so far make it possible to answer the questions submitted.

4. Examination of the questions submitted

54. *A* — The first question of interpretation raised by Article 27 is whether that provision permits only the adoption of special measures for combating tax avoidance where there is an *intention* to escape the tax or whether its scope also extends to cases in which avoidance appears to be an *objective* consequence of the

7 — See the declaration set out in the minutes of the Council meeting at which the Sixth Directive was adopted, which is referred to by the United Kingdom in its observations and which was referred to by the Court in paragraph 26 of its judgment of 10 April 1984 in Case 324/82 *Commission* v *Belgium* [1984] ECR 1861, at p. 1881.

trading practices adopted by the taxable person.

55. In that connection, the appellant companies contend that, apart from cases involving simplification of the procedure for charging the tax, Article 27 can apply only to cases of tax evasion.

56. In my view, that contention is incorrect.

57. The wording of Article 27 of the Sixth Directive — in all the language versions consulted, including the English version — clearly refers to two distinct concepts, that of tax *evasion* and that of tax *avoidance*, and expressly includes them within its scope, and the same applies to the seventeenth recital in the preamble to the directive.

58. In that recital, the directive departed from the wording of Article 13 of the Second Directive, which provided for the possibility of the adoption by the Member States of special measures only 'to prevent certain frauds'.

59. The difference in the wording makes it clear that the directive is now intended to include 'objective avoidance', thereby widening the scope of the permitted derogation.

60. The English-language version of the Sixth Directive is, it may even be said, particularly striking in that regard. Whilst the wording of Article 27 refers to the prevention of 'certain types of tax evasion or avoidance', the objective referred to in the seventeenth recital in the preamble to the directive is 'to avoid fraud or tax avoidance', thereby adding the latter concept (which corresponds to 'evasão fiscal' in Portuguese and to like terms in other Romance languages) to that of 'fraud', which was the only one referred to in the Second Directive.

61. The aim and the general scheme of that provision — as is clear from my previous exposition of the system established by the Sixth Directive — support that interpretation. Clearly, the possibility exists of adopting measures derogating from the general rules of the directive (in particular from Article 11 thereof). But, as I have emphasized, such derogations must, in view of their objectives and of the machinery selected, be in accord with the general spirit of the system of value-added tax.

62. Moreover, the solution adopted by the legislature in the Sixth Directive is understandable. To restrict the scope of the derogating measures to cases of evasion would not make it possible to achieve, to the same degree, the objectives of the directive, which would, moreover, be dependent on proof of fraudulent intent being furnished in each case; in addition, it would give rise to the possibility of discrimination between two companies, one of which had confined itself, with the intention of avoiding tax, to copying the trading methods introduced by the other even before the tax was created.

63. Reference may also be made, in support of the aforesaid interpretation, to the declaration mentioned earlier, contained in the minutes of the Council meeting at which the Sixth Directive was adopted, according to which the measures for preventing tax evasion or avoidance may consist, for instance, 'in provisions designed to prevent a decrease in the taxable amount which the Member State considers unjustified'.

64. That is also the view of the Government of the Federal Republic of Germany put forward in the observations submitted by it in these proceedings.

65. In my view, therefore, the conclusions which the two appellant companies have attempted to draw from a comparison between the wording of the Sixth Directive and that of the Second Directive are thereby weakened.

66. Nor do I consider that, under Community law as it stands at the present time, this detracts in any way from the spirit which inspires Article 19 of the Second Directive, whose objectives continue to be binding on the Community institutions with a view to the abolition of fiscal barriers within the Community, in accordance with Article 35 of the Sixth Directive.

67. *B* — Having regard to the system established by Article 27, the validity of a national measure derogating from the directive must be examined with reference to two distinct aspects.

68. The first aspect is concerned with the Council's *authorization*, which is required by Article 27 (1). The procedure described in Article 27 (2), (3), and (4) (notification of the Commission, provision of information to the Member States and express or tacit authorization) must have been properly complied with. Next, it is necessary to take into account the terms of the authorization and its relationship with the request.

69. Secondly, the validity of the measure depends on its compatibility with the *objectives* of Article 27 and with the general *principles* laid down by the Sixth Directive.

70. I propose to begin by considering the first of those two aspects.

71. As Mr Advocate General Verloren Van Themaat pointed out in his Opinion in the first *Direct Cosmetics* case,[8] the purpose of the various procedures laid down by Article 27 is to guarantee that 'no derogations from the normal system laid down in the directive (namely in Article 11) are made which do not meet the criteria laid down in Article 27'.

72. For that reason, Article 27 (2) provides that, when informing the Commission, a Member State wishing to introduce derogating measures must provide it with 'all relevant information'.

73. Those guarantees must also apply to national provisions which — like those at issue in this case — contain, for the benefit of certain administrative authorities, only a general authorization to adopt individual measures that are intended, in particular, to prevent tax evasion or avoidance. It would be unacceptable if, by adopting a purely general authorization enabling the competent authorities to derogate from the general system established by the Sixth Directive, the Member States avoided consideration of their measure in the light of the criteria laid down by Article 27 and permitted the adoption of individual implementing provisions which, not being so considered, might fail to satisfy those criteria.

74. If, moreover, the objectives of the provision in question and the circumstances in which it must be applied are not very

8 — [1985] ECR 617, at p. 626.

clear, it is only by considering all those elements taken together that the conclusion can be reached that the authorization granted is not a 'blanket authorization' and can therefore be assessed in the light of the criteria laid down by Article 27.

75. In that regard, I would point out that the wording of the contested measure now under consideration resulted from the repeal, in the version previously in force, of the phrase 'for the protection of the revenue', which may be regarded as equivalent to the phrase 'to prevent certain types of tax evasion or avoidance' used in the Sixth Directive.[9] That was the amendment which the Court examined in the first *Direct Cosmetics* case[10] and considered (in paragraph 27 of the judgment) to be of such a kind as to have severed any apparent link between the contested measures and the exceptions laid down in Article 27 (1).

76. The power of the Comissioners of Customs and Excise to derogate from the directive having thus been widened, to what would appear to be an indeterminate extent, the Court held (in paragraph 28 of the judgment) that a fresh notification was necessary, under Article 27 (2), in order to enable the Commission and, where appropriate, the Council 'to verify whether the new measure was still consistent with the aim laid down in paragraph (1) of that article'.

77. That was the notification effected by the United Kingdom on 15 March 1985, and it was on the basis thereof that the Commission and the Member States were able to verify the existence of such compatibility, which is the basis of the Council's tacit authorization.

78. Can the conclusion be drawn that the information provided with the notification was such as to enable the Commission and the Member States to make a comprehensive and informed assessment of the objectives, the scope and the nature of the measure, and to permit, as the national court asks, the validity of the tacit authorization granted to be recognized?

79. In that regard, I would point out in the first place that the notification effected by the United Kingdom authorities — which is set out in the order for reference — not only incorporates the text of the special measure for which authorization was sought but also contains various explanations regarding the objectives which it pursues, the origins and history of the legislation in question and the circumstances in which the measure is to be applied.

80. The notification refers, in particular, to the fact that 'in the United Kingdom certain companies, in the field of cosmetics for example, sell their products solely to retail dealers who are not required to be registered for VAT and are therefore outside the tax net. While these companies and dealers do not seek to evade payment of tax, the effect of their marketing structure is that tax on the value added by the dealer to the final consumer is avoided. Other companies selling similar products in direct competition and selling through normal registered retail outlets are therefore at a competitive disadvantage because the

9 — See paragraph 27 of the judgment of 13 February 1985 in *Direct Cosmetics*.

10 — Judgment referred to above.

price of their products to the final consumer bears additional VAT.'

81. The text of the notification also states that the measure in question is to be applied exclusively to large undertakings ('companies in a substantial way of business') which operate in the manner described, and that the measure will not be applied to other wholesalers selling to unregistered retailers.

82. In my view it is reasonable to conclude that a notification effected in those terms contains in substance all the information necessary to enable the addressees to understand its objectives and its scope and, in case of doubt or disagreement, to ask for the matter to be raised by the Council.

83. The observations submitted by the Council in these proceedings are to the same effect.

84. In those circumstances, the statement made by a United Kingdom member of Parliament during a parliamentary debate, which the appellants cited in support of their standpoint, is irrelevant.

85. C — In this case, however, the assessment of the problem is complicated by an anomalous factor.

86. Following the notification by the United Kingdom, the Commission, in compliance with Article 27 (3) of the Sixth Directive, informed all the Member States and the Council, by letters of 12 April 1985 and 9 July 1985 respectively, of the United Kingdom's application for derogating measures.

87. However, it was established that the English version of the Commission's communications used the term 'tax evasion', the English equivalent of 'fraude fiscal', and not 'tax avoidance' which, in the English-speaking world, corresponds more closely to 'evasão fiscal'.

88. The same terminology was used in the English text of the notice of authorization (85/369/EEC) published in the Official Journal of 31 July 1985 and would appear to have been repeated in two other language versions.

89. The Council detected the error and rectified it by publishing a corrigendum in Official Journal L 93 of 7 April 1987, at page 17. However, that error was not carried over into the text, published in the Official Journal, of the fresh grant of authorization to maintain the derogating measures in force for a further two years. [11]

90. The fact to which I have just referred is such as to raise doubts concerning the scope or the validity of the tacit authorization granted by the Council of Ministers and, consequently, on the scope of the derogating measure adopted by the United Kingdom.

91. In my view, however, that fact does not affect the legality of the procedure or, consequently, the validity of the measure adopted by the United Kingdom and the meaning which the United Kingdom evidently attributed to that measure in its notification thereof.

11 — Official Journal L 188 of 8 July 1987, p. 52.

92. All the Member States received, together with the Commission's letter, the text of the United Kingdom's notification setting out the details needed to enable them to understand, notwithstanding the terminological error or mistranslation, the scope of the measure concerned.

93. I would recall, in particular, that in the aforesaid notification, the United Kingdom authorities expressly pointed out that they were concerned with the situation of undertakings whose aim was not to escape the tax but whose commercial organization led to the tax being partially avoided.

94. Most of the language versions, including the French version, did not, moreover, as has been explained, contain the error in question. In addition, in its letter accompanying the text of the United Kingdom's notification, the Commission pointed out that it was tax avoidance 'by virtue of the pattern of distribution' that was intended.

95. Hence there is nothing to indicate that the Member States were misled with regard to the nature of the derogation sought since they had at their disposal all the information they needed in order to understand it.

96. Neither any of the Member States nor the Commission asked for the matter to be raised by the Council, with the result that, in accordance with Article 27 (4), the authorizing decision was deemed to have been adopted as from 13 June 1985. As the Council stated in its observations, it, as an institution, must be considered to have examined and agreed to the proposed measure.

97. It was that tacit authorization which was brought to public notice by publication in the Official Journal.

98. It is impossible, in my view, to arrive at any conclusion other than that such tacit authorization must inevitably have exactly the same scope and meaning as were attributed to it in the request for derogation submitted by the United Kingdom.

99. It would only be possible to alter the scope of a measure that was notified after the Council had assessed the notification and refused to grant the authorization sought.

100. Not only was the matter not raised by the Council but also none of the Member States subsequently contested — at least in the observations which they have submitted in these proceedings — the legality of the procedure in question on the basis of the aforementioned fact.

101. In those circumstances, it is impossible to see how the error could, in itself, affect the validity of the national measure adopted on the basis of the tacit authorization granted. If it were otherwise, the legitimate expectations of a Member State would be seriously frustrated and — as a result of an error for which it was in no way responsible — the legal position accorded to it by Community law would be adversely affected.

102. Nor is the position of the persons to whom the measures concerned apply adversely affected either. The national courts — which are responsible for applying national law — may always, in case of

doubt, request the Court of Justice, under Article 177 of the EEC Treaty, to provide them with an interpretation of Community law enabling them to review the legality of the procedure followed, which could be called in question if, for instance, the information needed to permit thorough scrutiny of the terms of the derogation sought had been withheld from the Commission or the Member States.

103. As we have seen, that was not the case in this instance.

104. *D* — I now turn to the second of the two aspects which I referred to earlier.

105. In their observations in these proceedings, the two appellant companies alleged, in the alternative, that the measure adopted by the United Kingdom was disproportionate in relation to the objectives which it sought to achieve and for that reason exceeded the limits set by Article 27 (1).

106. *(a)* In that connection, it is necessary to bear in mind, first and foremost, the approach taken by the Court in its judgment of 10 April 1984 in Case 324/82 *Commission* v *Belgium*,[12] according to which the special derogating measures that the Member States may maintain in force so as to prevent certain types of tax evasion or avoidance 'in principle may not derogate from the basis for charging VAT laid down in Article 11, except within the limits strictly necessary for achieving that aim'.

107. Earlier I explained that the general principle for determining the basis of assessment is, according to Article 11. A.1 (a), that such basis must comprise, in every transaction, the value of the consideration obtained by the supplier of the goods or by the person providing the services. Value-added tax is, historically, a consumer tax which is aimed, in principle, at the final consumer of the goods and is designed to impose a tax on him which is commensurate with his expenditure.[13] Hence the taxable amount is, as a rule, the real value of the transaction and not the presumed or open-market value.

108. For that reason, it is appropriate to ascertain the extent to which each derogating measure departs from the general definition of the taxable amount for value-added tax in order to determine whether it does so within limits that are strictly necessary.

109. In the case under consideration, the United Kingdom has explained that the result of the application of the measure in question was merely to permit the value added by certain categories of intermediaries to be taxed, so as to prevent tax avoidance and distortions of competition arising from the introduction in the marketing system of a further stage consisting in sales by agents not liable to tax.

12 — Cited above, paragraph 29 of the judgment.

13 — There is no need at this juncture to discuss the effect on the basic concept of value-added tax of introducing in Article 11. A.1 (a) of the Sixth Directive the reference to 'subsidies directly linked to the price of such supplies' and their inclusion in the consideration which constitutes the basis of assessment of the tax. That reference reflects a compromise in the directive between treating value-added tax as a business tax and as a consumer tax, which, in the former case, is charged on the value added to the cost of the components used and, in the latter case, is charged on the value added to market prices.

110. The United Kingdom argues that, in those circumstances, retailers are merely the taxable person's *alter ego*, in a scheme for sales direct to the public.

111. Having regard to the terms in which the measure itself is couched, it clearly applies only to cases in which the whole or a part of a taxable person's business (in fact, in the notification mention is made only of the taxable person's exclusive business) consists in supplying persons not liable to tax with goods which they are intended to sell by retail.

112. It must be acknowledged that, in those circumstances and in the absence of specially applicable measures, most or all of the goods sold by that taxable person would reach the public at a price which excluded the tax normally payable on the value added to the goods in question at the time when they are sold by the retailers.

113. The taxable amount would therefore no longer be the final value of a sale to the consumer since the difference between the final price and the price charged at the previous stage would escape taxation.

114. Conversely, if the goods were sold directly to the public by the taxable person, through his employees or through agents receiving a commission on sales, value-added tax would be charged on the full retail price on a sale to the final consumer. There would therefore be a distortion of competition which is contrary to the general system of value-added tax and which derogating measures of the kind under consideration are designed to prevent.

115. In the absence of such measures, that distortion of competition would even operate as an inducement to undertakings to change their trading methods, by using ostensibly independent retailers not liable to tax instead of agents paid on commission. That structural alteration would be brought about by the tax, which would lose its desirable neutrality.

116. The need for special measures is, it may even be said, particularly pressing in the case of the United Kingdom in view of the relatively high value of the exemption provided in that country for the benefit of small undertakings.

117. It may be said in that regard that — as the United Kingdom and the Commission have pointed out — the situation under consideration cannot be equated with that of a taxable person who makes normal sales to small undertakings within the limits of the exemption.

118. In the latter case, those sales account, in general, for only a small part of the turnover of the supplier, who usually sells through persons registered for tax purposes, and their volume is therefore negligible from the point of view of tax avoidance. On the other hand, the situations with which the derogating measures are intended to deal involve undertakings which sell exclusively or essentially in the manner described.

119. The United Kingdom has explained, moreover, that direct selling of consumer goods has grown considerably, representing

in 1985 a turnover of UKL 330 million, half of which was in the cosmetics and toiletries sector.

120. The conclusion may therefore be drawn that the purposes for which the United Kingdom sought authorization to adopt a derogating measure, rather than taking it outside the scope of Article 27, support the view that the measure is intended in principle to be in keeping with the general approach taken in the Sixth Directive.

121. *(b)* In addition, the request for authorization to adopt derogating measures was limited to a period of two years (subsequently extended by a further two years) and the United Kingdom undertook to study in the mean time the possibility of amending its national legislation in such a way as to achieve the same objectives without derogating from the provisions of the Sixth Directive.

122. *(c)* Moreover, it has not in my view been demonstrated that other solutions — such as those based on the second subparagraph of Article 4 (4) or the second subparagraph of Article 24 (3) — would always be workable or make it possible in all circumstances to achieve the same objectives just as effectively, even where all the preconditions therefor were satisfied.

123. As regards the mechanism provided for in the second subparagraph of Article 4 (4), its application depends on the fulfilment of a set of cumulative conditions. That provision applies to persons who, 'while legally independent, are closely bound to one another by *financial, economic* and *organizational* links' (emphasis added).

124. That description would not appear to cover every type of situation at which the United Kingdom's derogating measure is aimed. It clearly does not cover the situation in which Laughtons Photographs Limited finds itself and which is at issue in the main proceedings. The schools to which that company sells the photographs are independent entities and are not closely bound to the company by links of the kind required by the provision in question.

125. It is doubtful whether even the transactions concluded by Direct Cosmetics Limited could be regarded as coming within the scope of the aforesaid provision.

126. That fact is recognized by the Commission, which doubtless discouraged the United Kingdom authorities from resorting to that solution. The second subparagraph of Article 4 (4) would appear to constitute an exception to, or a derogation from, the definition of 'taxable person' which is given in Article 4 (1) and is explained, as regards the meaning of the word 'independently', in the first subparagraph of Article 4 (4).

127. It would seem, therefore, that, in so far as it contemplates the possibility of such an exception or derogation, the Sixth Directive was intended to permit special treatment to be accorded to entities which would otherwise be regarded as independent taxable persons.

128. That is the view that seems to be implicit in the explanatory memorandum in relation to the provision in question, as set out in the proposal for a Sixth Directive submitted by the Commission to the Council on 29 June 1973,[14] where it is

14 — Supplement 11/73 to the *Bulletin of the European Communities*, p. 8.

stated that 'in the interests of simplifying administration or combating abuses (for example, the splitting up of one undertaking among several taxable persons so that each may benefit from a special regime) Member States will not be obliged to treat as taxable persons those whose "independence" is purely a legal technicality'.

129. The companies whose links for the purposes of the application of value-added tax were considered by the Court in its judgment in *Van Passen* v *Staatssecretaris van Financiën*[15] were in the situation described above.

130. On the other hand, the agents of Direct Cosmetics Limited, who are employed by others at the places where they sell the products, supply their services to the company on a part-time basis during their free time and without being registered as persons liable to value-added tax.

131. In any event, it would not appear that the effects of the hypothetical application of that mechanism to an undertaking such as Direct Cosmetics Limited and to its agents would differ significantly from the effects of a derogating measure adopted in accordance with Article 27 and within the limits set by that provision.

132. As regards the possibility of relying upon Article 24 (3) and excluding the intermediaries in question from the special scheme envisaged for small undertakings, that is an option which involves matters of an administrative nature and considerations of economic policy, on which it is impossible for me to express a view in general terms. In certain cases, that solution may be more onerous or disproportionate than the measure actually adopted under Article 27, whilst in others that will not be so.

133. *(d)* However, the two appellant companies referred to another problem which is connected with breach of the principle of proportionality. That problem stems from the fact that in the notification it is stated that the derogating measure is to be applied only to companies 'in a substantial way of business', amongst those which operate in the manner described.

134. According to those two companies, it follows from the vagueness of that expression (which makes it necessary to define the scope of the term 'substantial business') that the authorization is too wide-ranging, which reduces the possibility of assessing the compatibility of the measure with Article 27.

135. In my view that is not necessarily the case. The reference in question seeks to restrict the application of the derogation to cases that are significant from the tax point of view and helps to restrict its use to cases where the tax avoidance which it is sought to prevent assumes serious proportions.

136. It is, to that extent, compatible with the approach manifest in the fact that Article 24 provides for schemes granting exemptions for small undertakings and the adoption or maintenance of such schemes by certain Member States.

137. It is important that the exercise of the resultant discretionary power should always

15 — Judgment of 12 June 1979 in Joined Cases 181 and 229/78 [1979] ECR 2063.

be subject to review by the competent judicial authorities, in order to ensure that its use is confined to the purposes for which the derogating measure was authorized and does not adversely affect taxpayers' rights or contravene any principle which must be upheld.

138. The fact that the United Kingdom legal system ensures sufficient legal protection in that respect has not even been disputed. Moreover, the United Kingdom has stated that the Commissioners of Customs and Excise issued instructions that the measure was to be applied only to undertakings whose annual turnover for value-added tax purposes exceeded UKL 50 000, which in any event helped to define the framework within which the discretionary power must be exercised.

139. *(e)* Therefore, it has not, in my view, been shown so far that the principle of proportionality can be properly relied upon in order to suspend the application of the contested measures.

140. However, the appellants also refer, in support of their view, to the judgment of the Court of 10 April 1984 in *Commission* v *Belgium.*

141. In paragraphs 31 and 32 of that judgment, the Court held that the Belgian legislation at issue, by applying to all new cars the catalogue prices notified to the Belgian authorities, entailed 'such a complete and general amendment of the basis of assessment that is impossible to accept that it contains only the derogations needed to avoid the risk of tax evasion or avoidance'. In particular, it had not been proved that, in order to attain the aim in view, it was necessary 'that the taxable amount should be fixed on the basis of the Belgian catalogue price or that the taking into account of any form of price discount or rebate should be excluded in such a comprehensive manner'.

142. In those circumstances, the Court concluded that 'the measures at issue are disproportionate to the aim in view in so far as they depart in a general and systematic way from the rules laid down in Article 11'.

143. The view may be taken — as it is by the United Kingdom — that that is not the case with regard to the measure now under consideration and that it applies only to certain specific selling schemes which lead to an undesirable reduction of the basis of assessment and result in 'tax avoidance'.

144. However, it remains to be determined whether the solution adopted — namely that of allowing the value of the transaction in those circumstances to be taken to be 'its open-market value [16] on a sale by retail' — resolves all the uncertainty regarding its scope and, consequently, its relationship of proportionality with the principles laid down by, and the objectives of, Article 27 and the Sixth Directive in general.

145. The derogating provision does not directly define what is to be understood by 'the open-market value' (in the original English version: 'its open-market value on a sale by retail').

146. The United Kingdom legislature must have borne in mind the concept of the 'open-market value' of a service, defined in the second subparagraph of Article 11. A.1, when it determined the basis of assessment

16 — Or its 'current' value.

in the case of services supplied by a taxable person for the purposes of his undertaking, within the meaning of Article 6 (3).

147. Thus, the directive treats the 'open-market value' of services as 'the amount which a customer at the marketing stage at which the supply takes place would have to pay to a supplier at arm's length within the territory of the country at the time of the supply under conditions of fair competition to obtain the services in question.'

148. That definition is comparable to that which the United Kingdom legislature adopted in section 10 (5) of the Value-added Tax Act 1983 and which is set out in the United Kingdom's observations.

149. Section 10 (2) provides that 'if the supply is for a consideration in money its value shall be taken to be such amount as, with the addition of the tax chargeable, is equal to the consideration' — a definition which seems to correspond to the general principle laid down by Article 11. A.1 (a) of the Sixth Directive — and section 10 (5) goes on to provide that:

'For the purposes of this Act the open-market value of a supply of goods or services shall be taken to be the amount that would fall to be taken as its value under subsection (2) above if the supply were for such consideration in money as would be payable by a person standing in no such relationship with any person as would affect that consideration'.

150. In that regard, it is appropriate to begin by pointing out that the reference in the second subparagraph of Article 11. A.1 of the directive to the 'open-market value' is clearly aimed at situations in which the service, as it is supplied 'for the purposes of [the taxable person's] undertaking', does not have a contractual price.

151. None the less, under the directive, a supply of services in those circumstances may be treated by the Member States (in accordance with the consultation procedure provided for in Article 29) as a supply of services for consideration for the purposes of applying the tax 'in order to prevent distortion of competition' which might arise in certain situations (Article 6 (3)).

152. In that case, the only way to determine the basis of assessment is by means of the open-market value, as defined in the second subparagraph of Article 11. A.1.

153. As regards the term 'open-market value' used in the United Kingdom legislation — both in Schedule 3 of Annex 4 to the Value-added Tax Act and in section 10 (5) thereof, which it is not appropriate to interpret here — it must be said that, whatever meaning it was intended to have in that act, its use is compatible with the objectives of the derogating measure and with the principles laid down by the Sixth Directive only in so far as it does not purport to impose tax on an amount exceeding the value added along the entire length of the distribution chain as far as the final consumer.

154. That means, in my view, that, if such a measure is not to be seen as excessive or disproportionate, the choice of a taxable

amount different from the consideration actually paid to the taxable person by the 'retailer' to whom the goods are supplied must not be based on anything other than the real price at which the goods are sold to the final consumer — or their open-market value if, and only if, it is impossible or excessively difficult to ascertain that price.

155. In the latter case, however, it must be the 'open-market' or 'current' value at which the goods reach the final consumer in transactions of the same kind.

156. That means transactions concluded in the same manner and involving goods of the same kind (for instance, cosmetic products which cannot be sold by other means and not products of 'standard quality' sold through the usual commercial channels).

157. It is that result which the national court must review when it is called upon to assess the manner in which the Commissioners of Customs and Excise have applied the authorization conferred upon them.

158. *(f)* I propose to use the cases of Direct Cosmetics Limited and Laughtons Photographs Limited to illustrate the two hypothetical situations, namely compatibility and incompatibility with Community law of the manner in which the measure is applied.

159. As regards Direct Cosmetics Limited, it is clear from the documents before the Court that the company began by selling its products direct to employees and workers in factories, hospitals and offices, and then decided (even before the derogating measure was introduced) to have recourse to the services of some of those employees who, as the company's agents, would sell the products to their colleagues in between office hours.

160. In both cases, it would appear, the products were to be supplied to the consumers at the company's catalogue price and, under the second of the schemes described, the agents' remuneration was to be a 20% commission which they could retain if they paid over the price to the company within 14 days.

161. In substance, therefore, there is no difference between the two methods as far as their economic consequences are concerned, and the derogating measure ensures appropriate fiscal treatment of the situation, within the value-added tax system, provided that the 'current market value' at the retail stage is regarded as the Direct Cosmetics catalogue price on sales to the public ('our price').

162. On the assumption that the agents do not sell the goods at a higher price, the imposition of the tax on a larger amount would clearly go beyond what is required by the objectives pursued by the derogating measure, namely the charging of the tax on the value which has actually been added to the goods by the time they reach the final consumer.

163. In the case of Laughtons Photographs Limited there would also appear to have been two successive, somewhat different, selling schemes.

164. Initially, the company granted the schools a 20% discount on the recommended retail price if they made payment to the company within 35 days.

165. After a time, the company changed to the procedure of invoicing each school at a price agreed with the school, and the latter sold the photographs to the children's parents at a price fixed by itself.

166. However, it is not clear whether the schools charge a price higher than the agreed price. They do so in certain cases and the proceeds, in general, go to the 'school fund'. In other cases, they simply charge the same price which they have to pay to the company.

167. It appears that, under both schemes, the schools pay only for the photographs actually sold.

168. In the case of both schemes, the application of a derogating measure of the kind provided for in the United Kingdom legislation is lawful only if its purpose is, in principle, to charge tax on the price actually paid by the final consumer.

169. Under the first scheme, in which the final price was known in advance, the measure in question would make it possible to prevent the 20% discount granted to the schools from escaping taxation.

170. The schools thus played a purely passive role as intermediaries without any commercial autonomy.

171. That would not appear to be the case under the second selling scheme. The schools retain their autonomy, they are not exactly an extension (*longa manus*) of the company and the price charged on the final sale to the pupils is not known in advance by the company.

172. However, if the real price can be determined, there is no justification, in my view, for taking the 'open-market value' of the goods as the taxable amount. That should only be done if it is impossible or extremely difficult to ascertain and tax the exact price charged, which constitutes the real consideration for the product supplied.

173. And in any event, only if no other solution (such as the one provided for in Article 24 (3) of the directive) proves to be less onerous.

174. If the schools were charged VAT on the transactions in question, that would doubtless impose less of a burden on the taxable person — the photographer — than would the application of the derogating measure to him. But it is necessary to consider whether that course of action is justified and is not itself disproportionate in relation to the objective pursued, account being taken in particular of the fact that the activities in question are sporadic, are of a merely ancillary nature as far as the schools' activities are concerned and, it would appear, are in most cases not profitable. This, however, is a question of fact which it is primarily the responsiblity of the national court to appraise in each individual case.

175. In any case, a measure which in the final analysis — on the basis of the 'current' or 'open-market' value — needlessly charged tax on a non-existent or merely

presumed basis of assessment would exceed the limits to which it is properly subject.

176. It must be borne in mind, above all, that the value-added tax system is not designed to prevent undertakings from using selling schemes such as those described earlier in order to rationalize and reduce costs, and consequently the derogating measures used to deal with such schemes cannot disregard the characteristics of the transactions involved.

5. Answers to the questions submitted

177. In those circumstances, I suggest that the questions submitted by the national court should be answered as follows:

'1. Article 27 (1) of the Sixth Directive permits the grant of authorization to the Member States for the adoption of special derogating measures to prevent certain types of tax avoidance, whether or not a fraudulent intention exists;

2. Article 27 (1) and the general principles laid down in the Sixth Directive do not prohibit a measure which departs from the basis of assessment defined in Article 11. A.1 (a) so as to levy tax on a taxable person whose business consists, wholly or in part, in supplying certain goods to unregistered retailers in respect of sales made by such retailers, provided that the taxable amount does not exceed the value at which the goods reach the final consumer in transactions of that kind, or their open-market value on a sale by retail where it is impossible to ascertain the
first-mentioned value, and provided that no other solution exists which is less onerous for the taxable person.

3. The Sixth Directive does not preclude the application of such a measure only to undertakings whose turnover exceeds a certain level.

4. The application of such a measure precludes the application of the general rule laid down in Article 11. A.1 (a) of the Sixth Directive.

5. Authorization for such a measure pursuant to Article 27 (4) must be deemed to be granted within the limits set by the information referred to in Article 27 (2), provided that such information contains all the details necessary for the Commission and the Member States to examine, without possibility of error, the objectives and the scope of the measure.'