JUDGMENT OF THE COURT
28 FEBRUARY 1984 [1]

Senta Einberger v Hauptzollamt Freiburg (reference for a preliminary ruling from the Finanzgericht Baden-Württemberg)

(Import turnover tax — Smuggled drugs)

Case 294/82

Tax provisions — Harmonization of laws — Turnover tax — Common system of value-added tax — Tax on importation — Application to the unlawful traffic in drugs — Not permissible — Criminal sanctions for offences — Power of the Member States
(Council Directives 67/228, Art. 2 and 77/388, Art. 2)

Illegal imports of drugs into the Community, which can give rise only to penalties under the criminal law, are alien to the provisions of the Sixth Directive on the harmonization of the laws of the Member States relating to turnover taxes — Common system of value-added tax: Uniform basis of assessment. Accordingly Article 2 thereof must be interpreted as meaning that no import turnover tax arises upon the unlawful importation into the Community of drugs which are not confined within economic channels strictly controlled by the competent authorities for use for medical and scientific purposes. That interpretation applies also to Article 2 of the Second Directive on the harmonization of value-added tax.

That finding is without prejudice to the powers of Member States to impose appropriate penalties in respect of contraventions of their drugs laws, with all the attendant consequences, in particular fines.

In Case 294/82

REFERENCE to the Court under Article 177 of the EEC Treaty by the Finanzgericht [Finance Court] Baden-Württemberg for a preliminary ruling in the action pending before that court between

1 — Language of the Case: German.

SENTA EINBERGER, Schallstadt-Wolfenweiler,

and

HAUPTZOLLAMT [Principal Customs Office] FREIBURG,

on the interpretation of Article 2 (2) of the Sixth Council Directive 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 (Official Journal 1977 L 145, p. 1),

THE COURT

composed of: J. Mertens de Wilmars, President, T. Koopmans, K. Bahlmann and Y. Galmot (Presidents of Chambers), P. Pescatore, Lord Mackenzie Stuart, A. O'Keeffe, G. Bosco, O. Due, U. Everling and C. Kakouris, Judges,

Advocate General: G. F. Mancini
Registrar: H. A. Rühl, Principal Administrator

gives the following

JUDGMENT

Facts and Issues

The facts of the case, the course of the procedure and the conclusions, submissions and arguments of the parties may be summarized as follows:

I — Facts and written procedure

1. By a final judgment of the Landgericht [Regional Court] Freiburg of

27 July 1977 Miss Senta Einberger, the plaintiff in the main proceedings, was given a suspended sentence of one year's imprisonment for infringement of the Drugs Law (Betäubungsmittelgesetz).

According to the findings of the Landgericht, Miss Einberger travelled on a number of occasions between the spring and autumn of 1974 to Basel in Switzerland and there sold to a Mr and Mrs Winiger a total of 280 grams of morphine in single lots of between 30 and 100 grams for a price of between Sfr 150 and 170 per gram. The morphine was unlawfully brought into the Federal Republic of Germany and was then taken to Switzerland by the plaintiff.

On the basis of Paragraph (2) of the Customs Law (Zollgesetz), the Hauptzollamt Freiburg, the defendent in the main proceedings, considered that the plaintiff should pay import duties on the quantities of drugs concerned because she had obtained smuggled goods after the liability to pay customs duty had arisen and before it had been extinguished, whilst she knew, or should have known, that the goods in question were subject to customs control. Consequently by notice of assessment of 19 January 1978, the Hauptzollamt claimed payment from the plaintiff of import duties in the sum of DM 10 960.30 (DM 5 712 customs duty and DM 5 248.30 turnover tax levied on imports).

The objection lodged by the plaintiff in the main proceedings against the notice of assessment was dismissed and she appealed to the Finanzgericht [Finance Court] Baden-Württemberg.

2. Referring to the judgment of the Court of Justice of 26 October 1982 (Case 240/81 *Einberger* [1982] ECR 3699), the Finanzgericht Baden-Württemberg, Außensenate Freiburg, Second Senate, by order of 29 October 1982, requested the Court to give a ruling on the following question:

"Is the imposition of import turnover tax on drugs compatible with Article 2 (2) of the Sixth Council Directive 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 (Official Journal 1977 L 145, p. 1 et seq.), if Member States are not permitted to levy customs duty?"

3. In the statement of grounds of the order making the reference, the Finanzgericht mentions that in the judgment of 26 October 1982 cited above the Court held that no customs duty may be levied on imports of morphine. It points out that the arguments against the lawfulness of the imposition of import turnover tax are essentially the same as those against the imposition of customs duty, namely that morphine could not, for example, be freely or legally marketed.

4. The order making the reference was received at the Court Registry on 17 November 1982.

Pursuant to Article 20 of the Protocol on the Statute of the Court of Justice, written observations were submitted by the German Government, represented by Martin Seidel and Ernst Röder, acting as Agents, by the French Government, represented by Jean-Paul Costes, acting as Agent, and by the Commission of the European Communities, represented by its Legal Adviser, Rolf Wägenbaur, acting as Agent.

Upon hearing the report of the Judge-Rapporteur and the views of the Advocate General the Court decided to open the oral procedure.

II — Written observations submitted to the Court

The *German Government* observes in the first place that the imports of drugs took place before or during the autumn of 1974 and that as a result the legislation applicable in this case is not the Sixth Council Directive of 17 May 1977 on the common system of value-added tax (uniform basis of assessment) but rather the Second Council Directive of 11 April 1967 concerning the structure and procedures for application of the common system of value-added tax (Official Journal, English Special Edition 1967, p. 16), which ceased to be effective only when the Sixth Directive entered into force. The German Government considers therefore that the question submitted for a preliminary ruling should be answered on the basis of the Second Directive.

It proposes that the Court's answer should be to the effect that the imposition of an import turnover tax on drugs must be compatible with Article 2 (b) of the Second Directive because that provision relates to all imports, whether or not they are lawful, a fact which is confirmed by the wording of Article 7 of the same directive. Only that interpretation is in keeping with the spirit and the objectives of the common system of value added tax, the purpose of which, as intended by the Council, is *inter alia:*

to levy a general tax on consumption;

to ensure that all goods bear the same charge regardless of their origin and channels of distribution;

to permit, with a view to ensuring neutrality in competition in international trade, full equalization at the frontier with regard to turnover tax, and

to implement the principle, which is applied throughout the world, whereby indirect taxes are levied in the State of destination.

Since the system is intended to ensure neutrality in competition regarding national and imported goods, the import turnover tax ought to correspond to the tax payable on domestic supplies of the same kind. In view of the clear terms of the provisions of the directive (see, on the one hand, Article 2 (b) in conjunction with Article 7 and, on the other, Article 2 (a) in conjunction with Article 5), unlawful transactions can escape turnover tax only pursuant to an express exempting provision. However, there is no provision of that kind (see Article 10 of the directive).

In the view of the German Government, the absence of any such exempting provision for prohibited transactions does not constitute a lacuna resulting from an omission on the part of the Council but derives from the principle that taxes must be fair, which prohibits more favourable tax treatment for unlawful acts than for lawful acts. The application of criminal-law provisions is not sufficient to combat the "underground economy" in particular because on occasion a person other than the criminal offender benefits from the unlawful activity. Moreover, in certain cases it is impossible to impose a penalty with the result that the competitive advantage arising from tax exemption continues to exist. The principle that an unlawful act must not enjoy more favourable tax treatment than a lawful act is laid down in German tax law in

Paragraph 40 of the Abgabenordnung (tax regulations) of 16 March 1976 which provides that:

"For the purpose of taxation, the fact that an act governed wholly or in part by a fiscal law infringes a legal obligation or prohibition or is contrary to public morals is irrelevant."

A fortiori that principle applies with respect to fiscal practice, in so far as the administration is in no position to verify whether any particular act is lawful. The German Government also emphasizes that according 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 ..."; for that reason, the fourth recital in the preamble to the Second Directive states that in order to enable the system to be applied in a simple and neutral manner, and to keep the standard rate of tax within reasonable limits, it is "necessary to limit special systems and exceptional measures".

Also, the German Government refers to the fact that Article 7 of the directive adopts the criterion of entry of the goods into a Member State and takes no account of what happens to them thereafter.

It also states that that interpretation cannot be rejected merely because, according to the case-law of the Court, customs duties may not be levied on the import of drugs. Whereas the essential purpose of customs duties is to provide protection against imports from non-member countries, turnover tax is characterized by fiscal interests and by the principles of equality and neutrality in competition. The obligation to pay turnover tax can always arise regardless of any customs debt, even though, by virtue of Article 7 (2) of the Second Directive, it may be linked with the obligation to pay customs duties.

Essentially, turnover tax forms part of a different system from that of customs duties since it plays a different role.

In the view of the German Government, Article 2 (b) of the Second Directive, as interpreted by it, that is to say to the effect that all imports, both lawful and unlawful, are subject to turnover tax, does not infringe any provision of Community law, in particular Article 95 of the EEC-Treaty, and has an adequate legal basis (Article 99 et seq. of the EEC Treaty).

Finally, the German Government argues that, by contrast with the case of customs duties, the Member States retain power to impose taxes on imports of drugs.

As a secondary point, the German Government maintains that the legal situation described above was not changed, as regards its result, by the entry into force of Article 2 (2) of the Sixth Directive, the content of which corresponds to Article 2 (b) of the Second Directive and which subject imports to value-added tax. Article 14 of the Sixth Directive provides no greater tax exemption for imports of drugs than the Second Directive.

The German Government therefore concludes that the imposition of import turnover tax on drugs is compatible with Article 2 (2) of the Sixth Directive.

The *French Government* on the other hand considers that the reasoning expounded by the Court in the two judgments concerning the imposition of

customs duties on the importation of drugs (see judgments of 26 October 1982 in Cases 221/81 and 240/81) should be transposed to the present case. The French Government refers therefore to the views which it put forward in those cases and to the fact that the Court held that no customs debt could arise in connection with the importation of a drug which could not be marketed and states that it does not appear that any other solution could be adopted with regard to a tax debt.

There are three reasons for this view:

In the first place, Article 2 (2) of the Sixth Directive clearly refers only to imports of goods which may be marketed. Secondly, Article 10 (3) thereof permits Member States to link the chargeable event and the date on which the value-added tax becomes chargeable with those laid down for customs duties and therefore the considerations regarding the uncertainty of the chargeable event apply in their entirety to the present case. Thirdly, in view of the rules for the collection of value-added tax on imports and the practice followed by the French authorities, a system under which total exemption from the customs and fiscal charges on drugs imported through clandestine channels is granted should be adhered to.

The French Government is of the opinion that although there is no express provision to that effect, it is apparent from any analysis of the provisions of the Sixth Directive, in particular Articles 5, 7, 9 and 10, that only the supply of goods and services and imports of goods which are not prohibited on grounds of public policy may be subjected to the charging of value-added tax.

The French Government also refers to the difficulty of determining the chargeable event where the drugs are not seized at the time of importation but have been disposed of or indeed consumed. If a tax debt should arise in such circumstances, it would depend merely on the success of inquiries and inspections. The French Government points out in that connection that the Court held in Case 240/81 that there is no justification for making a distinction, for customs purposes, between drugs which have not been discovered and those which are destroyed under the control of the competent authorities "since if such a distinction were made the application of customs duties would be subject to the chance of discovery" (paragraph 15 of the Decision).

The French Government also points out that an exemption from import turnover tax in no way encroaches upon the prerogative of Member States to take proceedings against those who commit offences and cannot prevent the imposition of value-added tax within the country on transactions involving unlawfully imported drugs which are subsequently put to lawful uses.

Finally, the French Government states that in Case 240/81 the Court limited the scope of its judgment to unlawful imports of drugs. It proposes therefore that the Court should rule that the import of drugs other than those intended for medical or scientific uses authorized by the Member States cannot give rise to the imposition of turnover tax.

The *Commission of the European Communities* states that in its opinion the question submitted is directly linked with Case 240/81 and to the findings of the Court in that case. It is therefore necessary to bear in mind in particular that the harmful nature of drugs such as morphine, heroin and cocaine is generally recognized and that the importing and marketing of them are for that reason prohibited in all the Member States, by virtue of the Single Convention on Narcotics, 1961, the only exception being a strictly controlled and limited trade which allows those products to be used lawfully for pharmaceutical and medical purposes.

The Commission considers in the first place that by virtue of Article 2 (2) of the Sixth Directive, the "importation of goods" is subject to value-added tax and in that connection it is of no significance whether the chargeable event is ascribable to the person paying the tax. The "importation" of goods takes place as soon as those goods enter the country within the meaning of Article 3. According to Article 10 (3), the chargeable event occurs and the tax becomes chargeable in respect of the importation as soon as the goods are brought into the country.

However, the Commission considers that it cannot be inferred therefrom that illegal imports are subject to import turnover tax. It points out that the Sixth Directive is based on Articles 99 and 100 of the EEC Treaty and is therefore intended to harmonize or approximate the laws of the Member States on turnover taxes "in the interest of the common market", and that objective entails reference to the aims pursued by the Community, as set out in Article 2 of the EEC Treaty, and to the action taken by the Community in order to secure, *inter alia,* in accordance with Article 3 (h), "the approximation of the laws of Member States to the extent required for the proper functioning of the common market". Imports of drugs into the Community which can give rise only to repressive measures fall wholly outside those objectives and guidelines, as the Court held in Case 240/81.

According to the Commission, the recitals in the preamble to the Sixth Directive confirm that the value-added tax system is intended to make it possible to pursue the objective of

"the effective removal of restrictions on the movement of persons, goods, services, capital and the integration of national economies" (third recital) "so that a common market permitting fair competition and resembling a real internal market may ultimately be achieved" (fourth recital).

The recitals in the preamble to the First and Second Directives on value-added tax are along the same lines. It follows that the unlawful importation of drugs is alien to the free movement of goods, the interpenetration of economies and the creation of a true internal market, in so far as it normally results in seizure of the goods and lawful trade (with the exception of officially permitted cases) is not possible. In consequence the unlawful importation of drugs which are not marketed in order to be used for medical or scientific purposes does not give rise to liability to payment of import turnover tax.

The Commission points out, finally, that in the area of turnover taxes and by contrast with that of customs duties the powers of the Community regarding harmonization are in fact limited to action in "the interest of the common market" or the functioning thereof, which makes it possible to take the view

that the question whether the unlawful importation of drugs must give rise to the imposition of value added tax is unrelated to the functioning of the common market and that unlawful importations of drugs fall wholly outside the scope of the Sixth Directive, so that the Member States retain the power to regulate that matter. However the Commission counters this by stating that such an interpretation of the applicable provisions of the directive would fail to take into account the exhaustive character of the Sixth Directive.

III — Answer to the question put by the Court

The Court invited the Commission to describe the provisions laid down by statute and regulation and the customs procedure applicable in each of the Member States in the case of a turnover tax debt arising in respect of the unlawful importation and marketing of drugs, and the tax legislation of each Member State dealing with any such tax debt. On 21 July 1983 the Commission submitted to the Court a table dealing with the legal position in the Member States.

IV — Oral procedure

At the sitting on 27 September 1983, oral argument was presented by the plaintiff in the main proceedings, represented by R. Endriss, Rechtsanwalt, by the German Government, represented by Ernst Röder, acting as Agent, and by the Commission, represented by R. Wägenbaur, acting as Agent.

The Advocate General delivered his opinion at the sitting on 22 November 1983.

Decision

1 By order of 29 October 1982, received at the Court Registry on 17 November 1982, the Finanzgericht [Finance Court] Baden-Württemberg referred to the Court for a preliminary ruling under Article 177 of the EEC Treaty a question on the application of turnover tax to smuggled drugs.

2 The dispute in the main proceedings concerns the determination of the turnover tax applicable upon the importation of quantities of morphine which, having been illegally imported into the Federal Republic of Germany, were sold in Switzerland in contravention of the Betäubungsmittelgesetz [German Drugs Law] by the plaintiff in the main proceedings. For those offences she was given a suspended sentence of one year's imprisonment by a German criminal court.

3 The Finanzgericht has raised the question whether the morphine is subject to turnover tax under Community law. It points out in that respect that, in its judgment of 26 October 1982 (Case 240/81 [1982] ECR 3699), the Court stated that the introduction of the Common Customs Tariff no longer left a Member State the power to apply customs duties to drugs which had been smuggled in and either destroyed as soon as they had been discovered or removed from the customs territory before discovery but did leave it full freedom to take criminal proceedings in respect of offences committed.

4 The Finanzgericht referred, as regards the facts of the case, to its findings in Case 240/81, namely that the morphine was not manufactured in the Federal Republic of Germany and that the quantity of that product sold by the plaintiff in the main proceedings had been smuggled into German territory in order to be illegally re-exported to a third country. The Finanzgericht refers to the above-mentioned judgment of the Court and asks whether the absolute prohibition of importation and marketing of drugs which prevents the application of customs duties also precludes the collection of turnover taxes on importation.

5 Having regard to those considerations, the Finanzgericht submitted the following question for a preliminary ruling:

"Is the imposition of import turnover tax on drugs compatible with Article 2 (2) of the Sixth Council Directive 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 (Official Journal 1977 L 145, p. 1), if Member States are not permitted to levy customs duty?"

6 It should be noted in the first place that the Finanzgericht refers to the Sixth Directive in its reference for a preliminary ruling, whereas it is apparent from the documents before the Court that the imports of drugs regarding which the national court is to give judgment took place in 1974, that is to say before the entry into force of that directive and therefore while the Second Directive applied (Official Journal, English Special Edition 1967, p. 16). However, it appears that there is no difference between those two directives as regards the essential issue in this case, either in the wording of the relevant provisions or in their context; consequently, the interpretation to be

given by the Court of Article 2 (2) of the Sixth Directive will apply equally to Article 2 (b) of the Second Directive.

7 Article 2 of the Sixth Directive, in defining the scope of value-added tax, mentions:

"1. The supply of goods or services effected for consideration within the territory of the country by a taxable person acting as such;

2. The importation of goods".

8 It is to be noted that the Sixth Directive contains a series of specific provisions covering all imports, that is to say imports into the Community both of goods from non-member countries and of goods from another Member State, those provisions being found in particular in Articles 3, 7, 10 (3), 11 (B), 14, 17 and 23 of that directive.

9 Thus, a distinction must be drawn between the transactions referred to in the first and second paragraphs of Article 2, which are based on different economic and legal considerations.

10 The court making the reference was therefore correct to relate the question submitted for a preliminary ruling only to Article 2 (2), that is to say to the importation of goods, and more particularly to the importation of goods from non-member countries, as indicated in the order making the reference. Moreover, the question submitted for a preliminary ruling does not concern the importation of illegal products in general but only the illegal importation of drugs.

11 In those circumstances, the question arises whether or not, in the absence of express provisions in the directive in regard thereto, the illegal importation of drugs constitutes a taxable transaction or whether the directive must be interpreted as leaving the Member States a power of decision in that respect.

12 In the first place it must be stated that the directive may not be interpreted as leaving that question outside its scope with the result that it would be for each of the Member States to decide that question for itself. Such an interpretation would be irreconcilable with the aim pursued by the directive which is to achieve far-reaching harmonization in that area, particularly with regard to the basis of assessment to value-added tax.

13 That having been established, it is also apparent from its context and objectives that the Sixth Directive precludes the levying of value-added tax on drugs when they are illegally imported into the Community. That conclusion is unavoidable, in view of the previous decision of the Court precluding the collection of customs duties in those same circumstances, by reason of the fact that the legal situation, represented in this instance by the chargeable event, is essentially the same in the two cases.

14 As regards the non-collection of customs duties when drugs are illegally imported, regard must be had to the decisions of the Court to the effect that when drugs are imported into the Community otherwise than through strictly controlled economic channels for use for medical and scientific purposes, no customs debt arises (see judgment of 5 February 1981 in Case 50/80 *Horvath* [1981] ECR 385, and the judgments of 26 October 1982 in Case 221/81 *Wolf* [1982] ECR 3681 and Case 240/81 *Einberger* [1982] ECR 3699).

15 The Court held that drugs not distributed through channels strictly controlled by the competent authorities for use for medical and scientific purposes were, by definition, subject to a total prohibition and marketing in the Community and that, for that reason, those drugs were not liable to customs duties where they remained within illegal channels, regardless of whether they were discovered and destroyed or were not detected by the authorities.

16 That reasoning cannot be confined to the collection of customs duties on importation but applies also to the collection of turnover tax on importation.

17 In that connection, it must be emphasized that the purpose of the directives on harmonization of the laws of the Member States on turnover taxes is to

establish a common system of value-added tax and in particular a uniform basis of assessment throughout the Community, just as the Common Customs Tariff establishes a Community régime for customs duties.

18 The two charges display comparable essential features since they arise from the fact of importation of goods into the Community and the subsequent distribution thereof through the economic channels of the Member States and since each constitutes a component of the sale price which is calculated in a similar manner by successive traders. Their parallel nature is confirmed by the fact that Article 10 (3) of the Sixth Directive authorizes Member States to link the chargeable event and the date when the turnover tax on importation falls due with those laid down for customs duties.

19 Moreover, in this case, for the purposes of both charges, the release of the goods in question into the economic and commercial channels of the Community is by definition absolutely precluded.

20 Accordingly, as the Court has already held in relation to customs duties on importation, illegal imports of drugs into the Community, which can give rise only to penalties under the criminal law, are wholly alien to the provisions of the Sixth Directive on the definition of the basis of assessment and, in consequence, to the origination of a turnover tax debt.

21 That finding is without prejudice to the powers of Member States to impose appropriate penalties in respect of contraventions of their drugs laws, with all the attendant consequences, in particular fines.

22 The reply to the question submitted must therefore be that Article 2 of the Sixth Directive must be interpreted as meaning that no import turnover tax arises upon the unlawful importation into the Community of drugs which are not confined within economic channels strictly controlled by the competent authorities for use for medical and scientific purposes. That interpretation applies also to Article 2 of the Second Directive.

Costs

23 The costs incurred by the German Government, the French Government and the Commission of the European Communities, which have submitted observations to the Court, are not recoverable. As these proceedings are, so far as the parties to the main proceedings are concerned, in the nature of a step in the action pending before the national court, the decision on costs is a matter for that court.

On those grounds,

THE COURT,

in answer to the question referred to it by the Finanzgericht Baden-Württemberg by order of 29 October 1982, hereby rules:

Article 2 of the Sixth Council Directive 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 (Official Journal 1977 L 145, p. 1) must be interpreted as meaning that no import turnover tax arises upon the unlawful importation into the Community of drugs not confined within economic channels strictly controlled by the competent authorities for use for medical and scientific purposes. That interpretation applies also to Article 2 of the Second Directive on the harmonization of value-added tax.

	Mertens de Wilmars	Koopmans	Bahlmann
Galmot	Pescatore	Mackenzie Stuart	O'Keeffe
Bosco	Due	Everling	Kakouris

Delivered in open court in Luxembourg on 28 February 1984.

P. Heim
Registrar

J. Mertens de Wilmars
President