JUDGMENT OF THE COURT (First Chamber)
28 May 1998 *

In Case C-3/97,

REFERENCE to the Court under Article 177 of the EC Treaty by the Court of Appeal (England and Wales) Criminal Division for a preliminary ruling in the criminal proceedings before that court against

John Charles Goodwin,

Edward Thomas Unstead,

on the interpretation of Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment (OJ 1977 L 145, p. 1),

THE COURT (First Chamber),

composed of: M. Wathelet, President of the Chamber, D. A. O. Edward and P. Jann (Rapporteur), Judges,

Advocate General: P. Léger,
Registrar: H. von Holstein, Deputy Registrar,

* Language of the case: English.

after considering the written observations submitted on behalf of:

— Mr Goodwin and Mr Unstead, by Alan Newman QC and Peter Guest, Barrister, instructed by Audrey Oxford, Solicitor, acting for Mr Unstead,

— the United Kingdom Government, by John E. Collins, Assistant Treasury Solicitor, acting as Agent, with Stephen Richards and Mark Hoskins, Barristers,

— the Greek Government, by Fokion Georgakopoulos, Legal Adviser to the State Legal Service, acting as Agent, and Anna Rokofyllou, Adviser to the Deputy Minister for Foreign Affairs, acting as Agents,

— the Commission of the European Communities, by Hélène Michard and Barry Doherty, of its Legal Service, acting as Agents,

having regard to the Report for the Hearing,

after hearing the oral observations of Mr Goodwin and Mr Unstead, represented by Alan Newman QC and Peter Guest, the United Kingdom Government, represented by John E. Collins, with Kenneth Parker QC and Mark Hoskins, the Greek Government, represented by Fokion Georgakopoulos and Anna Rokofyllou, and the Commission, represented by Barry Doherty, at the hearing on 15 January 1998,

after hearing the Opinion of the Advocate General at the sitting on 12 March 1998,

gives the following

Judgment

1 By judgment of 24 December 1996, received at the Court on 9 January 1997, the Court of Appeal (England and Wales) Criminal Division referred to the Court for a preliminary ruling under Article 177 of the EC Treaty a question on the interpretation of Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment (OJ 1977 L 145, p. 1; hereinafter 'the Sixth Directive').

2 That question was raised in criminal proceedings against Mr Goodwin and Mr Unstead, who were charged with the fraudulent evasion of VAT in respect of sales of counterfeit perfume products.

3 According to the documents before the Court, Mr Goodwin was accused of having purchased counterfeit perfume products and of having sold them without being registered for VAT. Mr Unstead was accused of having participated in the manufacture, production, distribution and sale of counterfeit perfume products through a business organisation which he ran together with other persons, and which was not registered for VAT.

4 At first instance, the case came before the Inner London Crown Court, which held that the Sixth Directive did not preclude the charging of VAT on the manufacture, production, distribution and sale of counterfeit perfume products, and found both defendants guilty of conduct contrary to section 72(1) and (8) of the Value Added Tax Act 1994.

5 Mr Goodwin and Mr Unstead have appealed against that decision to the Court of Appeal, arguing *inter alia* that Community law precludes the levying of VAT in a situation such as theirs.

6 The Court of Appeal believes that, as a matter of Community law, VAT is payable on supplies of counterfeit perfume products for consideration. However, being somewhat doubtful on the point, it stayed proceedings in order to refer the following question to the Court of Justice for a preliminary ruling:

'Does the supply of counterfeit perfume products fall within the scope of Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes (the Sixth Directive)?'

7 The crux of the question is whether, on a proper construction of Article 2 of the Sixth Directive, VAT is payable on the supply of counterfeit perfumes.

8 Article 2 of the Sixth Directive provides:

'The following shall be subject to value added tax:

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.'

9 It should be borne in mind at the outset that, according to established case-law, the Sixth Directive, whose purpose is to achieve widespread harmonisation in the area of VAT, is based on the principle of fiscal neutrality. As regards the levying of VAT, that principle precludes a generalised differentiation between lawful and unlawful transactions, except where, because of the special characteristics of certain products, all competition between a lawful economic sector and an unlawful sector is precluded (see *inter alia* Case C-111/92 *Lange* v *Finanzamt Fürstenfeldbruck* [1993] ECR I-4677, paragraph 16).

10 Referring to a number of judgments — Case 294/82 *Einberger* v *Hauptzollamt Freiburg* [1984] ECR 1177, Case 269/86 *Mol* v *Inspecteur der Invoerrechten en Accijnzen* [1988] ECR 3627, Case 289/86 *Happy Family* v *Inspecteur der Omzetbelasting* [1988] ECR 3655 and Case C-343/89 *Witzemann* [1990] ECR I-4477 — Mr Goodwin and Mr Unstead submit that, since there is no lawful market in counterfeit perfumes, the present case falls within the scope of that exception. In the United Kingdom, not only would a contract for the sale of counterfeit perfumes be void for illegality, but such sales would also infringe a wide variety of intellectual property rights. Furthermore, the placing of such products on the market seriously undermines the functioning of the common market inasmuch as, unlike narcotics, trade in counterfeit perfumes is never permitted.

11 In *Einberger*, *Mol* and *Happy Family*, the Court ruled that no turnover tax arises upon the unlawful importation into the Community of drugs or upon the unlawful supply of similar products effected for consideration within a Member State, in so far as the products in question are not confined within economic channels strictly controlled by the competent authorities for use for medical and scientific purposes. In paragraph 20 of *Witzemann*, the Court held that its reasoning in relation to the illegal importation of drugs applies *a fortiori* to imports of counterfeit currency.

12 In those four judgments, the Court added that unlawful imports or supplies of goods such as those at issue in those cases, release of which into the economic and commercial channels of the Community is by definition absolutely precluded and which can give rise only to penalties under the criminal law, are wholly alien to the

provisions of the Sixth Directive (*Einberger*, paragraphs 19 and 20; *Mol*, paragraph 15; *Happy Family*, paragraph 17; and *Witzemann*, paragraph 19). That line of case-law thus concerns goods which, because of their special characteristics, may not be placed on the market or incorporated into economic channels.

13 However, that is not the position here. As the Greek Government, the United Kingdom Government and the Commission emphasised, the goods at issue in the main proceedings are not goods which cannot be placed on the market because of their intrinsic nature or special characteristics.

14 As the Advocate General pointed out in point 22 of his Opinion, although transactions involving counterfeit products infringe intellectual property rights, any consequential prohibition is not linked to the nature or essential characteristics of such products, but to their detrimental impact on the rights of third parties. Similarly, as the Commission noted in its observations, the prohibition on counterfeit products, which stems from the fact that they infringe intellectual property rights, is conditional, not absolute as in the case of narcotics or counterfeit currency. That prohibition is not sufficient, therefore, to place trade in such products outside the scope of the Sixth Directive.

15 Furthermore — as the Commission also pointed out — the possibility of competition between counterfeit products and goods which are lawfully traded cannot be ruled out in a case such as that before the national court, in so far as there is a lawful market in perfume products on which counterfeit goods have a specific impact. Accordingly, such goods cannot, like narcotics or counterfeit currency, be regarded as *extra commercium*.

16 It must therefore be stated in reply to the question referred that, on a proper construction of Article 2 of the Sixth Directive, VAT is payable on the supply of counterfeit perfumes.

Costs

17 The costs incurred by the Greek and United Kingdom Governments and the Commission of the European Communities, which have submitted observations to the Court, are not recoverable. Since these proceedings are, for the parties to the main action, a step in the proceedings pending before the national court, the decision on costs is a matter for that court.

On those grounds,

THE COURT (First Chamber),

in answer to the question referred to it by the Court of Appeal (England and Wales) Criminal Division by judgment of 24 December 1996, hereby rules:

On a proper construction of Article 2 of Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonisation of the laws of the Member States relating to turnover taxes — Common system of value added tax: uniform basis of assessment, VAT is payable on the supply of counterfeit perfumes.

Wathelet Edward Jann

Delivered in open court in Luxembourg on 28 May 1998.

R. Grass

Registrar

M. Wathelet

President of the First Chamber