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The Concepts of Similarity and Indirect Protection under EEC Treaty Article 95: the Alcohol Cases

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NOTE

THE CONCEPTS OF SIMILARITY AND INDIRECT PROTECTION UNDER EEC TREATY ARTICLE 95: THE ALCOHOL CASES

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INTRODUCTION

The European Economic Community (EEC or Community) was created in response to the massive devastation of Europe in the

aftermath of World War II.[1] Destruction of all trade barriers among the European nations in order to create a common market was viewed as an integral part of the strengthening of Europe.[2] Article 2 of the Treaty of Rome (Treaty) sets out the principles of the EEC:

> The Community shall have as its task, by establishing a common market and progressively approximating the economic policies of the Member States, to promote throughout the Community a harmonious development of economic activities, a continuous and balanced expansion, an increase in stability, and accelerated raising of the standard of living and closer relations between the States belonging to it.[3]

One of the purposes of the Common Market is to create a single economic unit in which the sector that produces a particular good most efficiently will do so while driving out less efficient industries. This maximizes the use of scarce monetary, raw material, and labor resources. For example, assuming that there are no trade barriers, if the Italians can produce grapes more cheaply than the Germans, they will do so and export the grapes to Germany. Conversely, Germany may be able to export cars if it can produce them more efficiently and cheaply than the other Common Market states. The static effects of interaction[4] occur when this free movement of goods alters supply and demand patterns to maximize the welfare of the consumer.[5] The second purpose is to create a larger market in which economies of scale and mobility of the factors of production exist.[6] These economic effects are referred to as the dynamic effects of integration.[7]

Article 3 of the Treaty lists the spectrum of Community activities designed to accomplish these goals:

> [T]he activities of the Community shall include . . .

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1. For an excellent review of the circumstances leading to the formation of each of the European Communities, see E. STEIN, P. HAY & M. WAELBROECK, EUROPEAN COMMUNITY LAW AND INSTITUTIONS IN PERSPECTIVE 1-13 (1976).

2. The six original countries in the EEC were France, the Federal Republic of Germany, Italy, Belgium, The Netherlands, and Luxembourg.

3. Treaty Establishing the European Economic Community, March 25, 1957, art. 2, 298 U.N.T.S. 11 [hereinafter cited as EEC Treaty].

4. I. WALTER, THE EUROPEAN COMMON MARKET 1 (1967).

5. *Id.*

6. *Id.*

7. *Id.*

(a) The elimination, as between Member States, of customs duties and of quantitative restrictions on the import and export of goods, and of all other measures having equivalent effect;
(b) the establishment of a common customs tariff and of a common commercial policy towards third countries;
(c) the abolition, as between Member States, of obstacles to freedom of movement for persons, services and capital;
(d) the adoption of common policy in the sphere of agriculture;
(e) the adoption of a common policy in the sphere of transport;
(f) the institution of a system ensuring that competition in the common market is not distorted;
(g) the application of procedures by which the economic policies of Member States can be coordinated and disequilibria in their balances of payments remedied;
(h) the approximation of the laws of Member States to the extent required for the proper functioning of the common market.[8]

It must be noted that these provisions serve to effectuate the movement of goods within a market without obstacles to their free flow; there is no reference to the member states' internal taxation systems. A member state could thus impose an internal tax discriminating against goods coming from outside that member state. The tax measures contained in articles 95 to 99 of the Treaty are designed to avoid circumvention through internal tax regulations.[9] These provisions are not set out in the part of the

8. EEC Treaty, *supra* note 3, art. 3.

9. Article 95 is the main focus of this paper and will be discussed in detail in the text.

Article 96 prohibits the Member State's repayment of internal taxes on an exported good to a greater extent than the total it was originally taxed. *Id.* art. 96.

Article 97 provides:

> Any Member States which levy a turnover tax calculated on a cumulative multi-stage system may, in the case of the internal charges imposed by them on imported products or of drawbacks granted by them on exported products, establish average rates for specific products or groups of products, provided that such States do not infringe the principles laid down in Articles 95 and 96.
>
> Where the average rates established by a Member State do not conform with the above-mentioned principles, the Commission shall issue to the State concerned appropriate directives or decisions.

Id. art. 97.

Article 98 does not allow export subsidization by refunding internal taxes that are not indirect taxes without the approval of the Council. *Id.* art. 98.

Article 99 calls on the Commission to propose harmonization of the Member

Treaty detailing the provisions on customs duties and quantitative restrictions and entitled "Foundations of the Community," but rather in a portion of the Treaty entitled "Policy of the Community." This would seem to indicate that the tax provisions are not as important as the provisions presented in the "Foundations" section. Without the tax provision, however, the other portions of the Treaty calling for the free movement of goods would be ineffectual.

The European Court of Justice (Court) has held that the purpose of the Treaty's tax provisions is to fill in the gaps left by the provisions on customs duties and quantitative restrictions and to facilitate the establishment of free trade in goods within the market.[10] Article 95 of the Treaty is the provision most often invoked to achieve this purpose:

> No Member State shall impose, directly or indirectly, on the products of other Member States any internal taxation of any kind in excess of that imposed directly or indirectly on similar domestic products.
>
> Furthermore, no Member State shall impose on the products of other Member States any internal taxation of such a nature as to afford indirect protection to other products.[11]

Article 95 applies to products of the Member States,[12] and it can be invoked directly by the citizens of the Member States[13] to prohibit use of internal taxes to accomplish goals prohibited by the customs duties and quantitative restrictions. The application of article 95's provisions has, however, created some difficulties. The Treaty contains no definition of the terms "similar domestic products" or "indirect protection." Identifying similarity is a par-

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State's turnover taxes, excise duties, and other forms of indirect taxation. Upon the submission of the proposal, the Council can take action only by a unanimous vote. *Id.* art. 99.

10. In *Sociaal Fonds voor de Diamantarbeiders v. S.A. Ch. Brachfeld & Sons*, the Court stated: "Article 95 . . . is designed to fill the loopholes that tax measures might open up in the prohibitions by prohibiting the imposition on imported products of charges that are higher than those imposed on domestic products." 1969 C.J. Comm. E. Rec. 211, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8078.

11. EEC Treaty, *supra* note 3, art. 95.

12. Milkwerke Wohrmann v. Hauptzollamt, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8065 at 8007.

13. Firma Alfons Lutticke v. Hauptzollamt, Saarlovie, 1966 C.J. Comm. E. Rec. 257, [1961-1966 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8045.

ticularly difficult problem because it requires the drawing of a line. Since similar does not mean identical, the requisite degree of identity between two items sufficient to meet the Treaty's requirement of similarity cannot be clearly identified. And, even if the products are not considered similar, the Member States' internal taxation system might afford "indirect protection to other products."[14] Again, there are several problems in identifying the situations in which indirect protection is afforded. How great must the tax differential be to provide protection? How closely related must the products be? The European Court of Justice has attempted to deal with these problems, but questions still remain. Recently a number of actions were brought before the Court by the EEC Commission. These cases involved the domestic taxation system for alcoholic beverages and gave the Court another chance to examine the provisions of article 95.[15]

II. The Relationship of Article 95 to Other Treaty Provisions

A. *Article 95, Customs Duties, and Quantitative Restrictions*

In order to fully understand the role of article 95 in common market transactions, it is necessary to comprehend all of the Treaty provisions dealing with customs duties and quantitative restrictions. Articles 9 through 17 of the Treaty set out the prohibition on customs duties or charges having equivalent effect.[16] Customs duties are forbidden irrespective of the reason for which

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14. EEC Treaty, *supra* note 3, art. 95.

15. The four cases are Commission v. France, 1980 C.J. Comm. E. Rec. 347, [1980-1982 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 8647; Commission v. Italy, 1980 C.J. Comm. E. Rec. 385, [1980-1982 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 8648; Commission v. United Kingdom, 1980 C.J. Comm. E. Rec. 417, [1980-1982 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 8651; and Commission v. Denmark, 1980 C.J. Comm. E. Rec. 447, [1980-1982 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 8649.

16. Article 12 provides: "Member States shall refrain from introducing, as between themselves, any new customs duties on importation or exportation or charges with equivalent effect and from increasing such duties or charges as they apply in their commercial relations with each other." EEC Treaty, *supra* note 3, art. 12. The placement of these provisions within the Foundations of the Community section establishes their importance. Sociaal Fonds voor de Diamantarbeiders v. S.A. Ch. Brachfeld & Sons, 1969 C.J. Comm. E. Rec. 211, [1967-1970 Transfer Binder] Common Mkt. Rep. (CCH) ¶ 8078.

they are imposed.[17] Any pecuniary charge, no matter how slight, that is imposed because an item has crossed a border violates the provisions of articles 9 through 17.[18] No discriminatory or protective effect need be shown to establish a violation.[19]

The purpose of these provisions is to establish the free flow of products in a transparent market within the Community. This transparent market is designed to encourage a more efficient and, therefore, stronger economic unit.

Articles 30 through 37 of the Treaty prohibit the imposition of quantitative restrictions[20] such as quota systems. These provisions are qualified by article 36,[21] which allows exceptions in cases involving public morality, security, or policy; or the protection of health, national treasures, or industrial property rights. Again, the purpose of these provisions is to promote the free flow of goods among the Member States. Because of the important policy implications involved, the Court has been unwilling to make liberal use of the article 36 exceptions.[22]

The interrelationship between article 95 and the other articles must be examined. The Court has made it clear that article 95 and the provisions on customs duties cannot both be applied at once to the same factual situation.[23] The Treaty establishes dif-

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17. EEC Treaty, *supra* note 3, art. 12.

18. Commission v. Italy, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8079.

19. *Id.*

20. Article 30 provides: "Quantitative restrictions on importation and all measures with equivalent effect shall, without prejudice to the following provisions, hereby be prohibited between Member States." EEC Treaty, *supra* note 3, art. 30.

21. Article 36 reads:

> The provisions of Articles 30 to 34 inclusive shall not be an obstacle to prohibitions or restrictions in respect of importation, exportation or transit, which are justified on grounds of public morality, public order, public safety, the protection of human or animal life or health, the preservation of plant life, the protection of national treasures of artistic, historical or archaeological value, or the protection of industrial and commercial property. Such prohibitions or restrictions shall not, however, constitute either a means of arbitrary discrimination or a disguised restriction on trade between Member States.

Id. art. 36.

22. *See* Commission v. Italy, 1970 C.J. Comm. E. Rec. 187, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8057.

23. Firma Alfons Lutticke v. Hauptzollamt Saarlovie, 1966 C.J. Comm. E. Rec. 257, [1961-1966 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8045.

ferent schedules for the implementation of these provisions, indicating that they are intended to operate independently.[24] Because of the differences in schedules and matters of proof, situations in which article 95 applies must be differentiated.[25] A quantitative restriction and a tax imposed in violation of article 95 can be differentiated because the quantitative restriction implies a quota, whereas article 95 deals with monetary charges on the products.

A more difficult problem arises in differentiating taxes prohibited by article 95 from customs duties and charges having equivalent effect. In *Firma Deutschmann v. Federal Republic of Germany* the Court held that article 95

> cannot be applied to charges that are imposed at the time of or by reason of importation, that affect only a product imported from another Member State but not the domestic product, and that alter the price of the former so that the charges have the same effect on the free movement of goods as does a customs duty.[26]

In another case the Court held that domestic taxation is not a charge having the equivalent effect of a customs duty.[27] The determination of whether something is covered under article 95 or the customs duties provisions focuses on the implementation and effect of the charge. Customs duties are importation charges imposed at the border, while article 95 taxes are domestic charges imposed under a system of taxation affecting both domestic and imported goods. But the designation of the charge in national legislation is not controlling; courts also will consider the actual application of the charge.[28]

Article 95 fills the gap left by the provisions of the Treaty on customs duties, charges having the equivalent effect of customs duties, and quantitative restrictions. Under these provisions a Member State is not allowed to restrict the importation of another Member State's products. The system of prohibitions in the Treaty covers the remaining gamut of mechanisms that might be

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24. *See* Firma Deutschmann v. Federal Republic of Germany, 1965 C.J. Comm. E. Rec. 601, [1961-1966 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8035.

25. *See id.*

26. *Id.*

27. Sociaal Fonds voor de Diamantarbeiders v. S.A. Ch. Brachfeld & Sons, 1969 C.J. Comm. E. Rec. 211, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8078.

28. A. EASSON, TAX LAW AND POLICY IN THE EEC 10 (1980).

used to disrupt the free flow of goods among the Member States. But the lack of certainty engendered by the ambiguous wording of article 95 highlights the importance of the Court's interpretation of the provisions of article 95. An intrepretation allowing the Member States too much latitude in imposing domestic taxation systems could lead to the destruction of the entire free trade structure established by the Treaty, thus creating an article 95 loophole. On the other hand, the existence of dissimilar goods that are not in competition cannot be disputed. These competing considerations must enter into the Court's decisions.

B. *The Effect of EEC Harmonization Efforts on the Application of Article 95*

The Commission has recommended that harmonization of the Member States' tax laws on alcohol, wine, and beer, but the Council has refused to take any action to implement the recommendations,[29] despite article 99 of the Treaty which provides:

> The Commission shall consider how the legislation of the various Member States concerning turnover taxes, excise duties and other forms of indirect taxation, including countervailing measures applicable to trade between Member States, can be harmonized in the interest of the common market.
>
> The Commission shall submit proposals to the Council, which shall act unanimously without prejudice to the provisions of Articles 100 and 101.[30]

In *Hansen v. Hauptzollamt*[31] the Court addressed the issue of the effect of harmonization efforts on article 95 in the context of a preferential tax on certain forms of alcohol:

> At the present state of its development and in the absence of any unification or harmonization of the relevant provisions, Community law does not prohibit Member States from granting tax advantages, in the form of exemption from or reduction of duties, to certain types of spirits or certain classes of producers. Indeed, tax advantages of this kind may serve legitimate economic or social purposes, such as the use of certain raw materials by the distilling industry, the continued protection of particular spirits of high

29. For a discussion of EEC harmonization attempts under article 99, see [1975] COMMON MKT. REP. (CCH) ¶ 3201.

30. EEC Treaty, *supra* note 3, art. 99.

31. 1978 C.J. Comm. E. Rec. 1787.

quality, or the continuance of certain classes of undertakings such as agricultural distilleries.[32]

This ruling established that the Member States are free to create tax systems preferring certain goods as long as harmonization has not taken place. The Court continued, however, to indicate that any tax advantages given to a certain good or producer must be extended to all similar goods and producers of the other Member States without discrimination.[33] Lack of harmonization, therefore, has very little effect on the applicability of article 95. The Member State may create tax systems supporting certain goods, but the advantages granted must be extended in a nondiscriminatory fashion as required by article 95.

III. Concepts of Similarity and Indirect Protection

The first and second paragraphs of article 95 provide a disjunctive approach to the prohibition of certain forms of domestic taxation. The first paragraph provides an exact mathematical standard. The impact is that a violation of article 95 occurs if the imported and domestic goods are similar and the domestic taxation system imposes a higher charge on the imported good. The only determinations a Court need make to find an article 95 violation are whether the goods are similar and whether a higher tax rate is imposed on the domestic product. The second paragraph of article 95 provides a different standard to be used in assessing article 95 violations. The Court must determine whether the other product is being indirectly protected. This determination is based on an economic rather than mathematical standard and is, therefore, more difficult to define.

A. *Historical View of Similarity*

Because "similarity" is not defined in the Treaty, the Court of Justice has been forced to define the concept on a case-by-case basis. In *Firma Fink-Frucht v. Hauptzollamt*,[34] the Court held that products are similar within the meaning of the first paragraph of article 95 if they "are normally, for tax, tariff, or statistical purposes, as the case may be, placed in the same classifica-

32. *Id.* at 1806-07.

33. *Id.* at 1807.

34. 1968 C.J. Comm. E. Rec. 327, [1967-1970 Transfer Binding] Common Mkt. Rep. (CCH) ¶ 8069.

tion."[35] This is a neat, judicially manageable test for similarity under which an objective determination of similarity can be made by attempting to fit the products within the applicable classifications.

The Court applied another objective test in *Commission v. Italy*,[36] stating that products are similar if they "fall . . . in the same tax classification."[37] It is difficult, however, to determine the Court's exact meaning because the Court did not explain which tax classification should be decisive. If the tax classification of the offending country is decisive, any Member State could alter its system of taxation to make very few imported products similar to domestic ones.[38] The logical explanation is that the Court was once again applying the standard established in the *Fink-Frucht* case. The Court looks to how the product is normally classified for tax purposes, which means that the tax system of the offending state is only one of the classifications considered.

The Court provided more factors by which a determination of similarity can be based in its decision in *Rewe-Zentrale v. Hauptzollamt*.[39] This decision indicates that the existence of a particular raw material in two products does not necessarily make them similar, even when the tax in question is based on the amount of that raw material in the goods.[40] But the characteristics of the goods at the same stage in production or marketing is a factor in determining similarity.[41] Another important factor is whether the products meet similar consumer needs.[42] In addition to these factors, the Court cited the *Fink-Frucht* position that the classification of the product under the Common Customs Tariff is an important factor to be considered.[43]

Rewe added several new, less easily discernible considerations

35. [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8069 at 8039.

36. 1970 C.J. Comm. E. Rec. 187, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8088.

37. [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8088 at 8297.

38. *See* A. EASSON, *supra* note 28, at 26 n.48.

39. 1976 C.J. Comm. E. Rec. 181, [1976 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8343. The case dealt with the imposition of an excise tax known as the "Monopolausgleichspitze" by the Federal Republic of Germany on imported Italian Vermouth.

40. 1976 C.J. Comm. E. Rec. at 194.

41. *Id.*

42. *Id.*

43. *Id.*

to the similarity equation. No longer could the determination be made simply by looking to customs duty tables or statistical classification systems. Future decisions would be based on subjective consumer views and the similar characteristics of the products. Still, the customs and statistical classifications would continue to play a major role. The benefits of this shift away from reliance on official classifications are significant. The Common Customs Tariff was created as part of the external policy of the EEC to levy duties on products coming into the market from nations outside the market. The policy considerations relevant in setting up such duties might not be relevant in making a similarity determination within the market.[44] There is little doubt that the member states had no intention of tying themselves into definitions of similarity by creating the tariff system.[45]

The other factors considered by the *Rewe* Court, however, lack the objective precision of the tariff test. The consumer use factor may include all consumers in the Community, in the Member State, or in the world. The similar characteristics test also poses a problem. Saying that "similar" means "similar characteristics" begs the question presented by article 95, paragraph 1. The Alcohol Cases provided the Court with the opportunity to review these standards.

B. *Historical View of Indirect Protection*

Paragraph 2 of article 95 is meant to compliment the provisions set out in paragraph 1 of that article.[46] Even if the domestic good is not similar to the imported good, the second paragraph may make the Member State's tax provisions illegal as prohibitions on taxes affording indirect protection to other products. The Court of Justice has had less to say about the application of paragraph 2 than paragraph 1, but in *Fink-Frucht* it said that indirect,

> protection is given particularly if an internal charge imposed on an important product is higher than the charge on a domestic product that is in competition with it in one or more possible economic uses, without, however, meeting the conditions for similarity

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44. *See* A. EASSON, *supra* note 28, at 26.

45. *See id.*

46. Firma Fink-Frucht GmbH v. Hauptzollamt München-Landsbergerstrasse, 1968 C.J. Comm. E. Rec. 327, [1967-1970 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8069.

. . . .[47]

Thus, the test is whether the products are in competition. The exact meaning of the term "competition" is extremely difficult to ascertain. One suggestion has been that the Court is referring to substitutability[48]—whether the two products can be substituted for one another. This is obviously not what the Court intended, because substitution can be given such an expansive meaning that almost every product will be in competition with every other product.[49] Exactly what the Court did intend, however, is not clear. The Court of Justice addressed the application of article 95, paragraph 2, in its recent decisions on the *Alcohol Cases*.

IV. THE ALCOHOL CASES

On August 7, 1978, the EEC Commission brought a series of suits before the European Court of Justice against France,[50] Italy,[51] Denmark,[52] and the United Kingdom.[53] Although the facts of the cases differed, each involved alleged violations of Treaty article 95. The potentially violative taxation systems involved domestic taxes on different forms of alcohol. The court struck down the systems of three of the four member states and deferred its decision in the case against the United Kingdom.

A. *Commission v. France*

In the years in question, seventy-four percent of French production was taxed at the lowest rate applicable to spirits created from wine and fruit. Geneva, a French-produced product made from cereals, also was taxed at a lower rate than imposed on all other spirits manutactured from cereals.[54] In *Commission v.*

47. *Id.*

48. A. EASSON, *supra* note 28, at 33.

49. *Id.*

50. Commission v. France, 1980 C.J. Comm. E. Rec. 347, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8647.

51. Commission v. Italy, 1980 C.J. Comm. E. Rec. 385, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8648.

52. Commission v. Denmark, 1980 C.J. Comm. E. Rec. 447, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8649.

53. Commission v. United Kingdom, 1980 C.J. Comm. E. Rec. 417, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8651.

54. French total excise and manufacturing taxes were FF 7655 per hectolitre on spirits produced from cereals, FF 5975 per hectolitre on geneva, and FF 5125

France[55] the Commission accused France of violating article 95 by differentiating between genevas and other cereal-based spirits and of discriminating against cereal-based spirits as compared with wine derived spirits.[56]

1. The Commission's Contentions

The Commission argued that the prime function of article 95 is to break down the last remaining trade barriers within the Common Market.[57] Article 95 thus should be applied objectively with no consideration of social policy or the progress towards harmonization[58] because harmonization is ineffectual unless it occurs in the neutral marketplace article 95 was designed to create.[59] The Commission, indicated that harmonization actually had been slowed by the discriminatory tax systems of the Member States.[60] Member States' sovereignty in the area of internal taxation, according to the Commission, had been limited by the Treaty, so the Member States no longer had unlimited use of their systems of taxation for nonfiscal purposes.[61]

The Commission argued that all spirits are similar[62] within the meaning of article 95. It applied the standard that products are similar if they have the same characteristics and meet the same consumer needs.[63] The Commission felt that all spirits meet the

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per hectolitre on spirits produced from wine or fruit. Commission v. France, 1980 C.J. Comm. E. Rec. 347, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8647. Total French production of spirits was 1,230,000 hectolitres. These are the spirits listed under tariff subheading 22.09C of the Common Customs Tariff. 1980 C.J. Comm. E. Rec. at 349. Of this, 906,000 hectolitres were produced from wine or fruit; 8,000 hectolitres were genevas; and 312,000 hectolitres of rum were produced by the overseas French Departments. *Id.* at 350.

55. 1980 C.J. Comm. E. Rec. 347, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8647.

56. 1980 C.J. Comm. E. Rec. at 364.

57. *Id.* at 352.

58. *Id.*

59. *Id.* at 358.

60. *See id.*

61. "The tax sovereignty of the Member States has been considerably limited in the interests of intra-Community trade; those limitations relate in particular to the freedom for the national legislature to have recourse to a tax device in order to pursue extra-fiscal objectives." *Id.* at 352. The Court did not comment on the appropriateness of the Commission's contention.

62. *Id.* at 357.

63. *Id.* at 353.

same needs of consumers and, therefore, they should be taxed at the same rate.[64] Arguing that the chemical characteristics of the products are irrelevant, the Commission stated that the consumer use must be evaluated on the basis of use in the entire Community, rather than just the use in the member state whose tax system is under question.[65] Any other approach would result in a market fractionalized by barriers to free trade.[66]

The Commission used the Common Customs Tariff and the Brussels Nomeclature, both of which group all spirits together under one heading,[67] as a basis for its similarity determination.[68] Thus, the existence of subheadings or subclassifications in addition to the general classification for spirits is not relevant because the subheadings merely serve to effectuate the external commercial policy of the Community.[69] The Commission did not feel, however, that the same argument applied to the general classification of spirits, which may be used to evaluate similarity.

The Commission rejected taste and smell as tests to differentiate products under article 95, paragraph 1[70] because of the infinite variety of tastes and smells involved.[71] Again, the Commission emphasized that all spirits have characteristics that are sufficiently alike to meet the same needs of consumers.[72] It admitted that the various spirits are used in different ways, but argued that several different spirits can be suited for any given use and that there is no one spirit that cannot be replaced by at least one other.[73] Although the Commission based the thrust of its argument on article 95, paragraph 2, it argued alternatively that the French tax system violated article 95, paragraph 2, because it provided indirect protection to spirits obtained from wine.[74]

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64. *Id.*
65. *Id.* at 352-53.
66. *Id.*
67. *Id.* Subheading C of tariff classification 22.09 of the Common Customs Tariff applies to spirituous beverages.
68. *Id.*
69. *Id.*
70. *Id.* at 354.
71. *Id.*
72. *Id.*
73. *Id.*
74. *Id.* at 353-54. The Court's summary of the parties' contentions did not detail the Commission's article 95, paragraph 2, arguments. It is impossible to tell whether the Commission placed little emphasis on this part of the case or whether the Court merely failed to report the Commission's views.

2. The French Defense

France was unwilling to accept the Commission's reasoning. It felt that the *Hansen* case had established that, in the absence of harmonization, the Member States are free to set their own tax rates.[75] Even if the Member States are not free to set their tax rates without complying with article 95, France argued that the products involved in this particular case were not similar within the meaning of the first paragraph of article 95.[76] France found the subheadings under the general classification of spirits in the Common Customs Tariff helpful in establishing that the two products were not similar.[77]

In addition, France claimed that the products in question did not meet similar consumer needs. Consumers, argued the French, choose certain spirits for certain uses on the basis of the significant organoleptic differences among the spirits.[78] The French argued that there is a difference between a digestive, which is normally consumed after a meal, and an aperitif, which usually is consumed before a meal.[79] Some spirits are consumed straight, others on ice, and still others mixed. The French claimed that there was no similarity under article 95, paragraph 1 because they could find no substitutability.[80]

France argued that the second paragraph of article 95 did not apply because there is no competition between the spirits involved and because the difference in taxation is insufficient to provide protection to domestic goods.[81] Under the French cross-elasticity argument, there is no competition between the products because they are not interchangeable.[82]

Citing the particular facts of the case, France argued there was no protective effect created by French taxes.[83] Under the French system, spirits produced from wine are taxed at a rate that is only

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75. *Id.* at 355; *see* Hansen v. Hauptzollamt Flensburg, 1978 C.J. Comm. E. Rec. 1787.

76. 1980 C.J. Comm. E. Rec. 347, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8647.

77. *Id.*

78. *Id.* at 356.

79. *Id.* at 367.

80. *Id.* at 356.

81. *Id.*

82. *Id.*

83. *Id.*

six percent less than the rate on whiskey.[84] France argued that such a differential is minimal, especially in light of the differences between the products.[85] Pointing out that the consumption of cognac, a spirit produced from wine, had increased only thirty-five percent during the same period in which whiskey consumption had increased tenfold, France explained that these increases proved that no protection from wine-based spirits had existed during the period in question.[86]

3. The Court's Opinion

The major difference between the parties was that France argued that the Member States retain internal tax sovereignty until harmonization takes place, while the Commission insisted that article 95's provisions are directly applicable with no consideration of social or economic policy. Both parties agreed that similarity determinations should be based on consumers' needs, but the Commission felt that Community needs should be assessed on a Community-wide basis, while France argued that Community needs differed in each Member State. Both sides relied on the Brussels Nomenclature and the Common Customs Tariff, but the Commission focused on the larger, more general classifications while the French utilized the subheadings. France felt that organoleptic qualities should be a major factor in a similarity decision, while the Commission felt that the vague nature of these distinctions made them useless. The Commission argued that indirect protection is created by the French legislation, while France asserted that the products are not interchangeable and that the tax difference is too small to create a protective effect.

Faced with these conflicting views, the Court reemphasized[87] that the provisions of article 95 had been created to supplement the other articles involving customs duties, charges having the equivalent effect of customs duties, and quantitative restrictions.[88] The Court felt that the purpose of article 95 is to guarantee market neutrality.[89] In order to assure neutrality and equality, the similarity provision of article 95, paragraph 1, must be con-

84. *Id.* at 356-57.
85. *Id.* at 357.
86. *Id.*
87. *Id.* at 359.
88. *Id.*
89. *Id.*

strued broadly to cover all products, the taxation of which conflicts with the equality policy.[90] The products need not be identical.[91] The Court quoted *Rewe,* which relied on similar characteristics and consumer use of the product to establish the correct standard for similarity.[92]

The Court's interpretation of article 95, paragraph 2, echoed what had been said in the *Fink-Frucht* case: article 95, paragraph 2, applies when two products, even though not similar, are in competition with one another.[93] This competiton may be partial, indirect or potential.[94]

When applying article 95 to the Community market in alcohol, the Court said three distinct lines of thought must be taken into account:

> (a) it is impossible, first of all, to disregard the fact that all the products in question, whatever their specific characteristics in other respects, have common generic features. All are the outcome of the distillation procedure; all contain, as a principal characteristic ingredient, alcohol suitable for human consumption at a relatively high degree of concentration. It follows that within the largest group of alcoholic beverages spirits form an identifiable whole united by common characteristics;
> (b) in spite of those common characteristics, it is possible to distinguish within that whole products which have their own more or less pronounced characteristics. Those characteristics spring either from the raw materials used (in this connection it is possible to distinguish in particular spirits distilled from wine, fruit, cereals, and sugar-cane), or from manufacturing processes or, again from the flavourings added. Typical varieties of spirits may in fact be defined by these particular characteristics, so much so that some of them are even protected by registered designations of origin;
> (c) at the same time, it is impossible to disregard the fact that there are, in the case of spirits, in addition to well-defined products which are put to relatively specific uses, other products with less distinct characteristics and wider uses. There are, on the one hand, numerous products derived from what are known as 'neutral' spirits, in other words spirits of all origins including molasses alcohol and potato alcohol; these products owe their individuality only to flavouring additives with more or less pronounced taste. On the

90. *Id.*
91. *Id.* at 360.
92. *Id.* at 359-60.
93. *Id.* at 360.
94. *Id.*

> other hand, it is necessary to draw attention to the fact that in the case of spirits there are products which may be consumed in very different forms, either neat or diluted or, again, in the form of mixtures. These products may therefore be in competition with a range of varying size of other alcoholic products of more limited use. A characteristic of the three cases brought before this Court is however the fact that in each there are, in addition to well-defined spirits, one or several products with a broad range of uses.[95]

These considerations allowed the Court to make some preliminary findings. It pointed out that there are an indeterminate number of similar spirituous products, but the similarity may be difficult to ascertain because of factors such as flavor and consumer habits.[96] Even if similarity is difficult to identify the Court felt the numerous common characteristics of the products in these cases indicated at least partial or potential competition.[97] Even if the similarity between products is questioned, the competiton involved allows the invocation of the second paragraph of article 95:

> It appears from the foregoing that Article 96, taken as a whole, may apply without distinction to all the products concerned. It is sufficient therefore to examine whether the application of a given tax system is discriminatory or, as the case may be, protective, in other words whether there is a difference in the rate or detailed rules for levying the tax and whether that difference is likely to favour a given domestic product.[98]

The Court also pointed out the *Hansen* Court's treatment of the harmonization question, which emphasized that tax advantages may be granted only on nondiscriminatory bases.[99] Even though all harmonization efforts have failed, article 95 will apply.

Similar comments on the applicability of article 95 were repeated in two of the other three cases brought by the Commis-

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95. *Id.* at 361-62.

96. *Id.* at 362.

97. *Id.*

98. *Id.*

99. *Id.* at 363. In another recent decision, the Court reaffirmed its position in the *Hansen* case. Commission v. Italy, 1980 C. J. Comm. E. Rec. 1, [1981] COMMON MKT. REP. (CCH) ¶ 8631. The Commission argued that article 95 required the abolition of a discriminatory tax preference. 1980 C.J. Comm. E. Rec. at 12. The Court was unwilling to accept this and held that article 95 requires only that the Member State extend tax advantages in a nondiscriminatory fashion to all goods within the market. *Id.* at 13.

sion. In *Commission v. France*[100] the Court considered the arguments that the Common Customs Tariff and the Brussels Nomenclature provided a basis on which to make similarity determinations and found these arguments[101] inclusive.[102] The subheadings upon which the French proposed to base their similarity determinations were "designed with Community foreign trade in mind [and] cannot . . . constitute an appropriate classification from the point of view of the application to the present case . . . ."[103] This indicates a break from earlier decisions in which the Court placed a great emphasis on formal criteria. In this case the formal criteria suggested conflicting solutions, and although the Court criticized the French use of subheadings to determine similarity it was unwilling to make a choice between the solutions suggested by the more formal criteria.[104]

The Court could find no objective value to the French assertions that there is an important difference between a digestive and an aperitif,[105] or that legal distinctions can be drawn on the basis of flavor.[106] It pointed out that there is no such distinction in French law and that the distinction fails to account for the numerous uses for each of the various spirituous products, including uses that are unrelated to meals.[107] The Court felt that criteria based on the existence of numerous flavors were "too variable in time and space" to provide a valid basis for Community law.[108] Consumer habits varying from region to region also were rejected by the Court as being too vague to provide a valid legal distinction.

Having rejected the French classification and flavor arguments and the use of the Common Customs Tariff or the Brussels No-

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100. 1980 C.J. Comm. E. Rec. 347, [1980-1982 Transfer Binder] COMMON MKT. REP (CCH) ¶ 8647.

101. *See supra* text accompanying notes 67-69.

102. Commission v. France, 1980 C.J. Comm. E. Rec. at 368.

103. *Id.*

104. The Court pointed out that the subdivisions were particularly inapplicable because the French Code General des Impot is based on a classification system totally different from that of the Common Customs Tariff. *Id.*

105. *Id.*

106. *Id.* at 369.

107. The Court pointed out that article 406 of the French Code General des Impots does not classify spirits produced from cereal as aperitifs, but places aperitifs and digestives in the same group for the imposition of the manufacturing tax.

108. *Id.*

menclature as a basis for similarity determinations, the Court decided that it did not have to determine whether article 95, paragraph 1, applies because article 95, paragraph 2, prohibits the French system of taxation on spirits.[109] The Court found that the spirits in question are at least in partial competition because in some circumstances they provide alternative choices for consumers.[110]

To evaluate the protective nature of the tax, the Court compared the lower tax rate applied to a large percentage of the domestic production with the higher rate on imported products.[111] The imposition of a higher rate on one class of French spirits, those produced from aniseed, was not found to be relevant.[112] But the increase in the market share of whiskey did not convince the Court that the French taxes favoring spirits such as whiskey had no protective effect on the market.[113] The Court concluded that the French taxes on spirits violate the provisions of article 95 of the Treaty.[114]

B. *Commission v. Italy*

The situation in *Commission v. Italy*[115] was remarkably similar to that in *Commission v. France*.[116] Italy produces 400,000 hectolitres of spirits per year,[117] only 24,000 hectolitres of which are produced from fruit other than wine or marc.[118] An even smaller amount is produced from cereals.[119] The Italian tax on spirits is imposed in the form of tax banderoles on bottles of up to two litres.[120] A 1970 decree increased the tax banderoles rate on spirits obtained from cereals, while leaving the rate on spirits obtained from wine or marc at a considerably lower level.[121]

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109. *Id.*
110. *Id.* at 369-70.
111. *Id.* at 370.
112. *Id.*
113. *Id.*
114. *Id.*
115. 1980 C.J. Comm. E. Rec. 385, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8648.
116. *See supra* note 54.
117. 1980 C.J. Comm. E. Rec. at 387.
118. Marc is the residue remaining after the juice is pressed out of fruit.
119. Commission v. Italy, 1980 C.J. Comm. E. Rec. at 388.
120. *Id.*
121. *Id.*

The arguments presented by the parties were similar to those in *Commission v. France.*[122] Again the Court was unwilling to find that all the products involved were similar, but it did find enough common characteristics to provide an alternate choice for consumers in some circumstances.[123] The Court held that the provisions of paragraph 2 apply because the domestic products are taxed at a lower rate, whereas cereal-based spirits, almost all of which are imported, are subject to the higher rate.[124] The existence of minimal amounts of production of domestic spirits taxed at the higher rate was not sufficient to convince the Court that no protective effect existed.[125]

C. *Commission v. Denmark*

Only in the case of the products involved in *Commission v. Denmark*[126] was the Court willing to find similarity under paragraph 1 of article 95. It still based its holding, however, on the application of paragraph 2. Denmark produces seven million litres of spirits per year.[127] Eighty-five percent of this is aquavit[128] or schnapps,[129] while sixty-three percent to sixty-seven percent of the total Danish alcohol consumption is aquavit or schnapps. The other thirty-three percent consists of whiskey, vodka, cognac, gin, and rum, all of which are imported.[130] Danish tax legislation provides for one tax on aquavit and schnapps and a substantially higher tax for all other spirits.[131]

The arguments in *Commission v. Denmark* were similar to the arguments presented in *Commission v. France* and *Commission v. Italy,* and the Court's response was the same.[132] The Court applied paragraph 2 of article 95 and found violations of Community law.[133] In this case, however, the Court did find the existence

122. *See supra* text accompanying notes 57-86.
123. *See id.* at 407.
124. *Id.* at 408.
125. *Id.*
126. 1980 C.J. Comm. E. Rec. 447, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8649.
127. 1980 C.J. Comm. E. Rec. at 450.
128. Aquavit is a clear spirit flavored with caraway seeds. *Id.*
129. *Id.*
130. *Id.*
131. *Id.*
132. *See supra* text accompanying notes 56-80.
133. 1980 C.J. Comm. E. Rec. at 472.

of discrimination against similar products.[134] It found that spirits manufactured from neutral alcohol which we owe "their characteristic flavour to added flavouring extracts" are all similar to aquavit, which is also produced from neutral spirits.[135] Under this definition, vodka, gin, and geneva are similar products. The Court's willingness to make a similarity determination may have stemmed from the wording of the Danish legislation, which specifically defined spirits subject to the lower taxation as "[products] manufactured from neutral spirits and containing in their composition vegetable flavouring extracts . . . not resembling gin, vodka, geneva, wacholder, . . . liquer, punch, bitters, . . . aniseed spirits, rum, spirits distilled from fruit and other spirits whose typical taste is produced through distillation or maturation."[136] The Court felt compelled to assume that the Danish legislature had specifically listed certain products as being subject to the higher tax because the products were so similar to aquavit;[137] the Danish legislature used specific wording to avoid the confusion that might have resulted from the facial similarity of the goods. Thus, the words of the legislation may have forced a finding of similarity. Identifying what, if any, standard this provides for future decisions is difficult. The Court was clearly irritated by the Danish attempt to define all similar products, and it effectively thwarted the attempt. The decision may represent an effort to impose generic definitions on the legislation in this area. If a tax classification is created without listing specific products, the products may be similar. A generic, descriptive difference between the products must exist for a finding of nonsimilarity.

A passage in *Commission v. Denmark* suggests that the Court does not have to specify which standards form the basis for its decision:

> As regards most of the other alcoholic beverages subject under the Danish legislation to the highest rate of tax, it is impossible to establish with certainty how many of them are spirits which may be classified as "similar" to aquavit within the meaning of the first paragraph of Article 95 and how many of them are products which, although they cannot be classified as similar, are in competition or in the substitution relationship with aquavit which is referred to

134. *Id.* at 471.
135. *Id.*
136. *Id.* at 467.
137. *Id.* at 471.

by the second paragraph of the same article.

The Court considers that it is not necessary to give a ruling on this matter to resolve the present dispute. In fact, even if doubts remain as to the question to what extent the numerous alcoholic products classified by Danish legislation in the most heavily taxed tax categories must be considered as products similar to aquavit within the meaning of the first paragraph of Article 95, it is impossible reasonably to contest that all those beverages are without exception in at least partial competition with the product benefited by the Danish legislation.[138]

One question that has arisen is whether the provisions in the two paragraphs of article 95 can both apply to one situation. In *Commission v. Denmark* the Court has made it clear that the courts need not delineate whether paragraph 1 or paragraph 2 is the basis for the decision. One or both can apply. The Court's statement that it is impossible to determine how many of the different forms of alcohol are similar to aquavit is also interesting. Article 95, paragraph 1, seems to require such a determination by the Court. The Court may be creating a new, minimal standard based on the provisions of the second paragraph; if a violation of the second paragraph is found, there is no need to assess the applicability of the first paragraph. This is particularly important in light of the disparate analysis involved in applying each of the two paragraphs. The finding of a paragraph 1 violation requires precise mathematical analysis, while paragraph 2 violations are identified through more generalized economic analysis.

D. *Commission v. United Kingdom*

Unlike the other actions brought by the Commission, the case[139] against the United Kingdom was based solely on the provisions of article 95, paragraph 2. The case involved the tax rates on beer and wine, and the Commission made no attempt to establish the similarity of the two products. The United Kingdom produces very little wine, but it does brew a great deal of beer.[140] The Commission claimed that beer and wine are in competition with one another and that the United Kingdom's tax system violates article 95, paragraph 2,[141] by preventing the evolution of British personal preferences from beer towards wine. The Commission felt that the British tax could be proven discriminatory using any

138. *Id.* at 471-72.

139. Commission v. United Kingdom, 1980 C.J. Comm. E. Rec. 417, [1980-1982 Transfer Binder] COMMON MKT. REP. (CCH) ¶ 8651.

140. 1980 C.J. Comm. E. Rec. at 421.

141. *Id.* at 423.

one of several different measurement systems.[142] Wine is taxed at the rate of £ 3.25 per gallon, while beer is only taxed £ .613 per gallon.[143] The United Kingdom contested this method of comparison because it ignores the differences between wine and beer[144] and because it overlooks differences in the consumption of the two beverages.[145] The Commission suggested two other standards to combat these objectives that also establish the existence of a larger tax on wine than beer.[146] The first standard involved the relationship between the fiscal measure and the cost of the good.[147] Using this standard, the Commission argued that the British excise duty constitutes thirty-eight percent of the selling price of a bottle of wine, but only twenty-two percent of the price of beer.[148] The second test proffered by the Commission focused on the rate of tax on alcoholic content,[149] and the Commission showed that the British tax system still taxed wine fifty percent higher than beer.[150] In addition, between 1972 and 1977 the duty on beer increased fifty-nine percent and the duty on wine increased slightly over one hundred percent.[151]

The United Kingdom felt that the Commission had failed to understand the basic differences between wine and beer.[152] Wine, it argued, has three times more alcohol than beer; it is more expensive than beer; and wine and beer are not substitutes in the eyes of the citizens of the United Kingdom.[153]

The United Kingdom argued that the prices used by the Commission are unfair because they are based on the purchase price of beer and wine in retail stores.[154] Retail sales account for only ten percent of all beer sales and thirty-five percent of all wine sales.[155] According to the United Kingdom, a proper comparison

142. *Id.* at 425.
143. *Id.*
144. *Id.* at 427.
145. *Id.* at 428.
146. *Id.* at 425.
147. *Id.*
148. *Id.*
149. *Id.*
150. *Id.* at 435.
151. The duty on wine rose 102%. *Id.* at 426.
152. *Id.* at 427.
153. *Id.*
154. *Id.* at 428.
155. *Id.* at 429.

must be based on the total United Kingdom expenditures on each product. The tax thus constitutes twenty-three percent of the price of beer and twenty-four percent of the cost of wine.[156] The British argued that this difference is too small to provide protection for beer.[157]

The Court said that whether a competitive relationship exists under article 95, paragraph 2, depends on several policy and economic factors. Specifically, the Court must

> consider not only the present state of the market but also the possibilities for development within the context of free movement of goods at the Community level and the further potential for the substitution of products for one another which may be revealed by intensification of trade, so as fully to develop the complementary features of the Member States in accordance with the objectives laid down by Article 2 of the Treaty.[158]

This statement recognizes several policy issues. First, it makes it clear that only potential, and not present, competition need exist. Thus, even the possibility of the intensification of trade as the market matures constitutes competition. This loose definition certainly reflects the goal of encouraging free trade expressed in the Treaty. Any other approach could crystalize present consumer habits and prevent market unification.

Another purpose of the Community is to create an efficient economic system. The Court's discussion of the complementary features of the member states' economies emphasizes the economic aspects of the application of article 95, paragraph 2, with each state producing what it is best able to produce. The Commission need not provide statistical details to prove its case.[159]

The Court found that the Commission's assertion that there is substitution between wine and beer was correct.[160] Consumer habits of a particular region cannot be controlling, however, because arguing that they are controlling implies that they are so

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156. *Id.*

157. *See id.*

158. *Id.* at 432.

159. The Court said that "it is impossible to require in each case that the protective effect should be shown statistically. . . . [I]t is impossible to require the Commission to supply statistical data on the actual foundation of the protective effect of the tax system complained of." *Id.* at 433.

160. *Id.* at 434.

deeply entrenched that they could not be changed.[161]

The Court was willing to admit, however, that great differences exist between wine and beer, including price structures, manufacturing processes, and natural properties.[162] Price structure differentiations make it extremely difficult to compare the tax burdens on the two products. As a prerequisite to a decision,[163] the Court called upon the Commission to indicate the correct tax ratio between wine and beer.[164]

The Court offered guidelines to establish this tax ratio. Neither the use of volume nor the ordinary unit of consumption is the appropriate measure for comparison.[165] Comparing the tax burden against the selling price is also inappropriate because it is very easy to determine the price of a case of beer, but extremely difficult to do so for a case of wine due to great variations in cost.[166] The Court thus decided that alcoholic strength per unit volume is the only appropriate and objective means by which to compare the tax burdens on the products.[167] Using this measurement, wine is taxed more heavily than beer.[168] The Court concluded that the Commission showed a protective trend because taxes on wine had been increased greatly over a period during which the taxes on beer had not varied.[169]

While acknowledging the protective effect of the tax, the Court refused to reach a decision because "of the uncertainties remaining both as to the characteristics of the competitive relationship between wine and beer and as to the question of the appropriate tax ratio between the two products from the point of view of the whole Community . . . ."[170] The Court wanted the Commission to develop a tax ratio that would be applicable to taxes on wine and beer in the whole market, to reconsider the case in light of its opinion, and to present its observations at a later date.[171]

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161. *Id.*
162. *Id.*
163. *Id.* at 435.
164. *Id.*
165. *Id.* at 436.
166. *Id.*
167. *Id.*
168. *Id.*
169. *Id.* at 438.
170. *Id.*
171. *Id.*

V. An Analytical Framework

The Court's most recent statements on article 95 must be drawn together in a coherent structure. These cases laid to rest several questions but created several others. The *Hansen* language regarding the ability of the Member States to grant tax advantages to certain goods[172] was clarified in the *Alcohol Cases:* these advantages can be granted only if applied nondiscriminatorily to both foreign and domestic products.[173] The questions left unanswered by the *Alcohol Cases* cover a broad panorama involving the concepts of similarity and indirect protection.

A. *Similarity*

The *Alcohol Cases* provide only a hazy picture of the Court's new concept of similarity. Flavoured neutral spirits are all similar under the decision, but the Court's unwillingness to find similarity[174] indicates that all spirits are not similar.[175] On the other hand, the Court's refusal to find similarity may have been an attempt to provide leeway for future definitions of similarity.

It is clear that goods do not have to be identical before they fall within the ambit of article 95.[176] Indeed, the raw material content of the product is not conclusive.[177] The test is still whether the products meet similar consumer needs and have similar characteristics.[178] All the consumers in the common market will be considered to identify consumer needs rather than consumers in a particular region.[179]

The formal criteria that played such a large part in determining similarity in earlier cases have lost support. Indeed, if application of the formal criteria does not produce a clear answer as to whether the goods are similar, courts will probably refuse to consider the criteria.[180] Subjective determinations such as taste and smell will also be rejected because of vagueness.[181]

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172. *See supra* text accompanying notes 33 & 99.
173. *Id.*
174. *See supra* text accompanying notes 134-37.
175. *See* A. Easson, *supra* note 28, at 36.
176. *See supra* text accompanying note 91.
177. *See supra* text accompanying note 40.
178. *See supra* text accompanying note 92.
179. *See supra* text accompanying note 108.
180. *See supra* text accompanying notes 102-04.
181. *See supra* text accompanying note 108.

B. *Indirect Protection*

The existence of competition between given products is the test used to determine that a Member State's tax system violates the second paragraph of article 95.[182] Partial, indirect, or potential competition will suffice.[183] The ability to substitute one product for another is clearly competition,[184] but the potential reach of the substitution criteria is unclear. Statistics on the growth of the overtaxed product's share of the market and the existence of a domestic product taxed at the higher rate are not relevant[185] on the question of whether a protective effect exists.[186] In the *Alcohol Cases* the Court indicated that paragraphs 1 and 2 of article 95 can be used in conjunction.[187] Whether paragraph 2 will now become a minimal test with a concomitant decrease in the importance of the definition of similarity is still unclear. The emphasis on paragraph 2 may indicate a preference on the part of the Court for looking at the large economic issues that are involved in a paragraph 2 determination instead of the rather strict requirements of paragraph 1.

Commission v. Denmark suggests that bad legislative drafting may be the basis for a determination by the Court.[188] This argument by default based on poor drafting certainly differs from the precise analysis characterizing previous article 95, paragraph 1 cases.

The *Commission v. United Kingdom* case adds one significant problem to a paragraph 2 determination. In that case the Court focused on the proper tax ratio between the two competing products, whereas in the other cases a lower tax on a protected product gave rise to the presumption of an article 95 violation. In the *United Kingdom* case the Court stated that the taxes can be different on the two products as long as a Community-wide ratio has been established. One author has suggested that tax distinctions should only exist for dissimilar, and not similar, competing products.[189] Almost similar competing products should bear similar

182. *See supra* text accompanying note 93.
183. *See supra* text accompanying note 94.
184. *See supra* text accompanying notes 48 & 49.
185. *See supra* text accompanying note 113.
186. *See supra* text accompanying note 112.
187. *See supra* text accompanying note 97.
188. *See supra* text accompanying notes 136-38.
189. *See* A. EASSON, *supra* note 28, at 37.

taxes, while dissimilar products should be taxed to reflect the differences between the products[190] so that the tax system does not afford protection to one of the products because of the differences between the products.[191] In the *United Kingdom* case the Court suggested that this ratio be based on the alcoholic strength of the product.[192] If this is the proper interpretation of the Court's action, the Court will be forced to decide whether products are "almost similar" regardless of its determination not to invoke the provisions of paragraph 1. Again, the Court will be forced to draw a line, but it will be a line between two standards not even mentioned in the Treaty.

VI. CONCLUSION

The European Court of Justice's decision in the *Alcohol Cases* must be evaluated in the light of the policies of the Community. As discussed earlier, the purpose of the tax provision of the Treaty is to preserve the free trade within the Community created by the provisions on customs duties and quantitative restrictions. Free trade within the market benefits all concerned by creating a stronger, more efficient economic unit. In order to accomplish this goal, the provisions of article 95 were created to ensure a neutral market. In addition to article 95 and the provisions on free trade, article 99 was created to harmonize the laws of the Member States and further unify the market. Recent attempts of the Commission and the Council to harmonize the Member States' taxes on alcohol have been unsuccessful. Therefore, article 95 will be the main vehicle to reconcile Community taxes on alcohol.

Broad interpretation of the concepts of similarity and indirect protection assure that the case law perpetuates this neutral market. The similarity test used by the Court properly rejects the argument that the needs of consumers should be determined based on the needs of the consumers of a particular Member State. In rejecting this contention, the Court avoids the possibility of a crystalized market in which the needs of consumers are dictated by habit and tax legislation. The Court's rejection of subjective qualities such as taste and smell also effectuates the

190. *Id.*
191. *Id.*
192. *See supra* text accompanying notes 167-68.

policy of free trade within the Community.

The "competition" test used to determine whether article 95, paragraph 2, applies is also extremely broad. The determination that such competition need be only partial, potential, or indirect indicates the zeal with which the Court is acting to uphold the Community's free trade policy. The competition criteria are extremely vague, and substitutability, another ambiguous term, is the only factor cited by the Court as determinative that competition exists.

The Court's recent opinions in the *Alcohol Cases* indicate a willingness to create Community economic and social policy. The first signs of this willingness appeared in the Court's preference for the second paragraph of article 95 because interpretation of the second paragraph involves more general, economic analysis than that involved in a determination based on the first paragraph. Decisions based on paragraph 2 thus give the Court more latitude in decision making. It must be pointed out that the Court's preference for paragraph 2, however, may merely represent a response to the difficulties involved in comparing the hundreds of available types of alcoholic beverages.

Far more difficult to justify is the Court's requirement in the *United Kingdom* case that a Community-wide tax ratio be created for wine and beer. Admittedly, the provisions of article 95, paragraph 2, do provide a great deal of discretion in identifying indirect protection, but this would not seem to include a requirement that the Commission create a Community-wide tax ratio simply because it chose to bring an action against one particular state. Attempts by the Commission and the Council to harmonize taxes on alcohol have been clearly unsuccessful, but this does not justify Court-imposed harmonization on the Community. The determination of a tax ratio for wine and beer should be part of the harmonization procedure set out in article 99, which delegates the harmonization responsibility to the Commission and the Council. No mention is made of the Court. Harmonization decisions are more properly made by the political branch of the Community, and the Court's decision shifts this power to the bureaucratic and judicial branches.

The Court's broad interpretation of article 95 in the *Alcohol Cases* is necessary to ensure that free trade will continue among the member states, creating a stronger and more efficient economic unit. The Court must be careful, however, not to become involved in the legislative process of harmonization. The purpose

of article 95 is to facilitate development of a neutral market, not to unify national legislation, and the Court must be sensitive to this distinction.

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