OPINION OF MR ADVOCATE GENERAL JACOBS
delivered on 25 October 1990 *

My Lords,

1. This case comes to the Court by way of a reference for a preliminary ruling from the Finanzgericht München. It concerns the question whether customs duties and value-added tax (VAT) can be charged on the importation into a Member State of counterfeit banknotes. As such, it constitutes a sequel to a series of cases that arose out of attempts by the German and Dutch authorities to charge customs duties and VAT on transactions involving prohibited drugs.

2. The facts of the present case are straightforward. In June 1981 Mr Max Witzemann acquired counterfeit money with a face value of USD 300 000 in Italy. He then took it to Germany by car, intending to sell it in Munich. He was arrested in Munich and the counterfeit banknotes were seized. Three years later the Hauptzollamt München-Mitte issued a tax assessment requiring Mr Witzemann to pay customs duties and VAT on the counterfeit banknotes. It is not clear from the order for reference or the national case-file on what basis the German authorities purported to charge customs duties; possibly they took the view that the Community origin of the goods was not proven. I would in any event emphasize that customs duties may in principle be imposed only on the importation of goods into the customs territory of the Community from third countries.

3. Mr Witzemann challenged the assessment on the ground that it was contrary to Article 9 and Articles 12 to 29 of the EEC Treaty. He also cited certain judgments of the Court holding that customs duties and VAT cannot be charged on illicit transactions in prohibited drugs. He argued that the Court's case-law on drugs was equally applicable to counterfeit money.

4. The Finanzgericht München has referred the following question to the Court:

'Are the provisions of the EEC Treaty (Article 3(b), Article 9(1), Articles 12 to 29) and the Sixth Council Directive 77/388/EEC of 17 May 1977 on the harmonization of the laws of the Member States relating to turnover taxes (Article 2(2)) to be interpreted as meaning that a Member State is not entitled to impose customs duties and import turnover tax on illegally imported goods, the production and sale of which is — as in the case of

* Original language: English.

counterfeit currency — prohibited in all Member States?'

5. Before attempting to answer that question I shall briefly summarise the existing case-law. In Case 50/80 *Horvath* v *Hauptzollamt Hamburg-Jonas* [1981] ECR 385 the Court held that:

'... the introduction of the Common Customs Tariff no longer leaves a Member State the power to apply customs duties to drugs which have been smuggled in and destroyed as soon as they were discovered but does leave it full freedom to take criminal proceedings in respect of offences committed, with all the attendant consequences, including fines.'

6. In that case the prohibited drugs had been discovered and seized. It was not long before the same problem arose in a case in which the illegal importation remained undetected until after the drugs had been disposed of. The Court held, none the less, that the same principle applied and that no customs debt arose upon the importation of drugs otherwise than through economic channels strictly controlled by the competent authorities for use for medical and scientific purposes, regardless of whether the drugs were discovered and destroyed under the control of those authorities or went undetected by them: see Case 221/81 *Wolf* v *Hauptzollamt Düsseldorf* [1982] ECR 3681 and Case 240/81 *Einberger* v *Hauptzollamt Freiburg* (*'Einberger I'*) [1982] ECR 3699.

7. In Case 294/82 *Einberger* v *Hauptzollamt Freiburg* (*'Einberger II'*) [1984] ECR 1177, the Court held that the same principle applied to VAT. Illegal imports of drugs were wholly alien to the provisions of the Sixth Directive (Directive 77/388, Official Journal 1977 L 145, p. 1) and Article 2 thereof must be interpreted as meaning that VAT could not be charged on the unlawful importation into the Community of drugs.

8. Finally, in Case 269/86 *Mol* v *Inspecteur der Invoerrechten en Accijnzen* [1988] ECR 3627 and Case 289/86 *Happy Family* v *Inspecteur der Omzetbelasting* [1988] ECR 3655 the Court held that internal supplies of prohibited drugs were, like imports, not subject to VAT.

9. It will be clear from the above summary that the previous cases represent a natural progression. The Court began by holding that customs duties could not be charged on imports of prohibited drugs that had been seized and destroyed. It then held that the same rule applied to drugs that remained undetected and so were not seized. It went on to hold that the rule established for customs duties was also valid for import VAT. Finally, it held that the same rule applied to VAT on internal supplies. All the above cases were concerned with prohibited drugs, but here again there has been a natural progression. In *Horvath* the drug in question was heroin, the sale of which was prohibited in all the Member States; in *Happy Family* it was hashish, the sale of which, though illegal, was in fact tolerated by the national authorities of the Member State in question. The Court rejected

attempts to distinguish between 'hard' and 'soft' drugs and took the view that the above principles applied to all prohibited drugs covered by the United Nations 1961 Convention on Narcotics (see paragraphs 25 and 26 of *Happy Family*).

10. The question which arises in the present case is whether the principles developed in connection with drugs should be extended to counterfeit money. There are of course many other steps that could be taken along the same road. Illegality manifests itself in many forms and there are many products that either cannot be lawfully traded or trade in which is subject to certain restrictions: drugs, counterfeit money, weapons, pornography, the pelts of certain animals, stolen goods and so forth. Not every transaction tainted with illegality will be exempt from taxation. A line must be drawn between, on the one hand, transactions that lie so clearly outside the sphere of legitimate economic activity that, instead of being taxed, they can only be the subject of criminal prosecution and, on the other hand, transactions which, though unlawful, must none the less be taxed, if only for the sake of ensuring, in the name of fiscal neutrality, that the criminal is not treated more favourably than the legitimate trader.

11. Only the Commission has submitted written observations. It considers that the principles established in the Court's case-law on drugs must apply equally to counterfeit money. As in the case of certain drugs, the prohibition on counterfeit money is universal. Moreover, whereas there is a legitimate trade in drugs such as heroin (for medical and pharmaceutical purposes), there is no such trade in counterfeit money, except perhaps among collectors in very limited circumstances. However, the Commission states that it has always had reservations about the Court's case-law on drugs and points out that in the *Horvath* case it was in favour of charging duty on prohibited drugs. None the less, the Commission does not suggest that the Court's case-law should be called in question.

12. The Commission points out that there has been an important legislative amendment since the aforesaid cases were decided. Council Regulation (EEC) No 2144/87 on customs debt (Official Journal 1987 L 201, p. 15) has replaced Council Directive 79/623 (Official Journal 1979 L 179, p. 31). The regulation took effect from 1 January 1989 and did not of course apply at the time when the facts of the present case occurred. Article 2(2) provides as follows:

'The customs debt on importation shall be incurred even if it relates to goods subject to measures of prohibition or restriction on importation of whatever kind.

However, no customs debt shall be incurred on the unlawful introduction into the customs territory of the Community of narcotic drugs which do not enter into the economic circuit strictly supervised by the competent authorities with a view to their use for medical and scientific purposes. For the purposes of criminal law as applicable to customs offences, the customs debt shall

nevertheless be deemed to have been incurred where, under a Member State's criminal law, customs duties provide the basis for determining penalties, or the existence of a customs debt is grounds for taking criminal proceedings.'

It should be noted also that Article 8(1) of the regulation provides that a customs debt is extinguished by confiscation of the goods. Accordingly the legislation has introduced, in relation to goods other than narcotic drugs, within the second subparagraph of Article 2(2), a distinction which the Court decided not to draw in *Wolf* and *Einberger I*: such goods are subject to customs duties, but the customs debt is extinguished by confiscation.

13. The first subparagraph of Article 2(2) of the regulation states a general rule but the second subparagraph introduces an exception in line with the case-law of the Court. The Commission observes that the second subparagraph of Article 2(2) was inserted because there was some doubt whether the case-law on drugs rested on primary law — in which case it was binding on the legislature — or on secondary sources. Since the first possibility could not be excluded, it was decided to adopt legislation that accorded with the case-law of the Court, although the Commission and some Member States would have preferred a different solution. The Commission also states that during the process leading to the adoption of the regulation no one thought of the problem of counterfeit money; if anyone had thought of it, it would have been treated in the same way as prohibited drugs.

14. The Commission proposes that the Court's case-law on prohibited drugs should be extended to counterfeit money, but that the Court should make it clear that it bases its ruling on secondary sources of law, i. e. legislation, rather than on the Treaty itself. The legislation applicable to the present case would be the Common Customs Tariff, Article 2 of Directive 79/623 (the predecessor to Regulation No 2144/87) and, as regards VAT, the Sixth Directive. It should be noted, however, that the time-limit for the implementation of Directive 79/623 did not expire until 1 January 1982, so its applicability to the present case must be in doubt. But the issue is not of crucial importance, since the directive did not deal expressly with the question whether customs duties should be charged on illegal goods. In that respect there seems to be no major difference between the legislation applicable in the present case and the legislation applicable in the previous cases cited above.

15. The Commission is right to raise the question of the legal basis of the Court's case-law. It is important that the legislature should know to what extent it is free to intervene in this area. The present case presents the Court with a timely opportunity to clarify whether its case-law was founded on the Treaty itself, in which case it is beyond the reach of the legislature, or whether it was founded on secondary sources, in which case it can of course be amended by the legislature.

16. The *Horvath* judgment was founded mainly on the fact that the method of assessing duty laid down in the Common Customs Tariff and in Council Regulation (EEC) No 803/68 on the valuation of

goods for customs purposes (Official Journal, English Special Edition 1968 (I), p. 170) was based on the assumption that the imported goods were capable of being put on the market and absorbed into commerce. The Court was also influenced by the fact that Regulation (EEC) No 1430/79 on the repayment or remission of import or export duties (Official Journal 1979 L 175, p. 1) provided for the repayment of duty where the goods were destroyed under the supervision of the competent authorities. The only Treaty provision mentioned in *Horvath* was Article 18 of the EEC Treaty, which is not in my view directly relevant.

17. In *Wolf* and *Einberger I* the Court again referred to Regulation No 803/68 and also to the preamble to Directive 79/623 on customs debt. But the main ground of its judgments was that:

'The introduction of the Common Customs Tariff . . . falls within the scope of the objectives assigned to the Community in Article 2 [of the Treaty] and the guide-lines laid down in Article 29 for the operation of the customs union. Imports of drugs into the Community, which can give rise only to repressive [i.e. penal] measures, fall wholly outside those objectives and guide-lines.'

18. The ruling in *Einberger II* was based ostensibly on an interpretation of the Sixth Directive, but the Court's underlying concern seems to have been to ensure that VAT on imports was subject to the same rule as that which it had laid down for customs duties. The Court clearly felt that it would be illogical to apply different rules to two charges that displayed 'comparable essential features' (see paragraph 18 of the judgment). Echoing the language of the *Wolf* and *Einberger I* judgments, the Court held that:

'. . . 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' (paragraph 20).

19. In *Mol* and *Happy Family* the Court recognized that that reasoning applied equally to VAT on internal transactions (*Mol*, paragraph 16; *Happy Family*, paragraph 18). The Court also noted in *Mol* and *Happy Family* that the Sixth Directive was based on Articles 99 and 100 of the EEC Treaty and that its objective was the harmonization or approximation of the legislation of the Member States on turnover taxes 'in the interest of the common market' (*Mol*, paragraph 14; *Happy Family*, paragraph 16). The Court apparently felt that, if the purpose of harmonizing legislation on turnover taxes was to facilitate the free movement of goods, it was illogical to charge VAT on a type of commerce that the law of all the Member States sought to suppress.

20. I do not think that in any of the above judgments the Court ever intended to suggest that the rule against charging customs duties or VAT on the importation or sale of prohibited drugs was derived directly from the EEC Treaty or from some general principle of law and that it could not be changed by the legislature. Admittedly, the true basis of the rule is somewhat obscure. The Court has referred to both primary and secondary sources of

law. Its approach has been as follows: the legislation is silent on this particular point, so it is necessary to examine the Treaty provisions on which the legislation is based and to see if they provide any guidance. That is of course an appropriate technique of interpretation, but there is no reason to assume that the rule thus arrived at is a direct interpretation of the Treaty which is binding on the legislature and can be altered only by an amendment of the Treaty. Moreover, it cannot, I think, be suggested that there is any fundamental principle of law precluding the taxation of illicit transactions. I am therefore of the opinion that the Community legislature is free to intervene in this area and to provide, if it so wishes, that customs duties and VAT must be charged on narcotics and other prohibited products.

21. As to the question whether the legislation applicable to the facts of the present case should be construed as precluding the charging of customs duties and VAT on the importation of counterfeit money, I have no doubt that the principles established by the Court in relation to drugs were equally applicable, before the entry into force of Regulation No 2144/87, to counterfeit money.

22. It is true that the Court has always recognized that not all prohibited goods should be treated in the same way (see paragraph 9 of the *Horvath* judgment). In the present proceedings the Commission has rightly pointed out that the catalogue of prohibited products varies from one Member State to another and that the uniform application of the Common Customs Tariff and of the Sixth Directive would be jeopardized if each Member State refrained from charging customs duties and VAT on the particular products that happen to be prohibited under its own legislation. For that reason I question whether the rules established by the Court in relation to drugs should be applied to operations that are contrary to national legislation on, for example, trade in firearms, pornography or animal pelts. Such legislation varies considerably from one Member State to another. Moreover, there is normally a legitimate trade in such products that cannot clearly be distinguished from the illicit trade. For example, the same type of firearm can be bought and sold legitimately by an authorized dealer and unlawfully by a black-market supplier. It would be illogical to confer a fiscal privilege on the latter.

23. But such considerations do not apply to counterfeit money, which is subject to a prohibition at least as universal and fundamental as the prohibition on narcotics. Like drugs, counterfeit money is the subject of an international convention, namely the International Convention for the Suppression of Counterfeiting Currency (*League of Nations Treaty Series*, Vol. 111-112, 1930-31, Vol. CXII, p. 371). That Convention is binding on all the Member States except Luxembourg, which, though an original signatory, has not ratified it. It is none the less a criminal offence under Luxembourg law to manufacture or circulate counterfeit banknotes, including foreign ones (Criminal Code, Articles 173 to 178). Since the Convention has at least been signed by all the Member States, the position in this case is different from that in *Mol*, where the treaty in question, the Convention on Psychotropic Substances, 1971, had not been signed by some Member States, and therefore, according to the judgment

(paragraph 24), did not constitute a basis for the interpretation of Community law.

24. In some respects the arguments for excluding counterfeit money from the ambit of the Common Customs Tariff and the Sixth Directive are even stronger than in the case of prohibited drugs. Whereas certain drugs that are at present prohibited in all Member States may one day be legalized in some Member States, it is hardly conceivable that the prohibition on counterfeit money will ever be relaxed. Moreover, whereas there is a legitimate trade in drugs such as heroin for medical and pharmaceutical purposes, there is no such trade in counterfeit money. The Commission mentions the possibility of counterfeit banknotes being traded as collectors' items but even that seems to be excluded by the terms of the aforesaid international Convention, which requires counterfeit currency to be confiscated and handed over on request to the bank of issue whose currency is in question.

25. It follows from the foregoing that the considerations that inspired the Court's case-law on drugs apply equally to counterfeit money and that, before the entry into force of Regulation No 2144/87, the relevant legislation was to be interpreted as precluding the charging of customs duties and VAT on the importation of counterfeit money.

26. As to whether the importation of counterfeit money gives rise to a customs debt after the entry into force of Regulation No 2144/87, that question does not of course need to be answered in the present proceedings. In the interests of legal certainty, however, it may be useful to consider the question.

27. Article 2(2) of Regulation No 2144/87 provides that:

'The customs debt on importation shall be incurred even if it relates to goods subject to measures of prohibition or restriction of whatever kind.'

An exception is then made for 'narcotic drugs which do not enter into the economic circuit strictly supervised by the competent authorities with a view to their use for medical and scientific purposes'. The Commission suggested, at least in its written observations, that that exception could be applied by analogy so as to encompass counterfeit money, since the legislature would have provided similarly for counterfeit money if the matter had been considered.

28. I cannot agree with the Commission on this point. The wording of Article 2(2) is perfectly clear and I see no reason to force upon it a meaning that it cannot possibly have. It is not the task of the Court to rectify the omissions of the legislature or to speculate about what rule the legislature would have enacted if it had considered a particular matter that evidently escaped its attention. Moreover, in the field of customs law, where the need for legal certainty is paramount, there is no basis for interpreting legislation extensively by way of analogy in

the manner proposed by the Commission. I conclude therefore that, after the entry into force of the regulation, import duties are payable on the importation of counterfeit money into the customs territory of the Community. At the same time, I think it will be helpful for the Court to indicate in its ruling that its case-law on drugs extended to counterfeit money only until the entry into force of the regulation; that will make it clear that the case-law was not based on any superior rule of law but could be modified by legislation.

29. One final question that arises (though once again it does not need to be answered in the present case) is whether the link between customs duties and VAT on imports is so strong that, since the entry into force of Regulation No 2144/87, the importation of counterfeit money is subject not only to customs duties but also to VAT. It might be argued that VAT is payable whenever a customs debt is incurred. As the Court noted in *Einberger II*, Article 10(3), second subparagraph, of the Sixth Directive allows Member States to link the chargeable event and the date when VAT becomes chargeable with those laid down for customs duties. However, it seems to me that Article 10 is concerned only with the date on which the liability to VAT takes effect; it is not concerned with the question whether the liability exists or not. Moreover, Article 10(3) merely allows Member States to link VAT with customs duties for this purpose; it does not require them to do so. I do not think that the Sixth Directive establishes an absolute link between customs debt and VAT liability. The principle laid down by the Court in *Einberger II* excluding imports of prohibited drugs from the ambit of the Sixth Directive is equally applicable to counterfeit money and continues to apply notwithstanding the fact that Regulation No 2144/87 has made the importation of counterfeit money subject to customs duties. If the legislature considers that the result is to create an unacceptable anomaly between customs duties and VAT, the remedy must be to amend the legislation.

30. I conclude that the question referred to the Court by the Finanzgericht München should be answered as follows:

'Under the provisions of Community customs law in force until 1 January 1989, when Council Regulation No 2144/87 took effect, the unlawful importation of counterfeit money into the customs territory of the Community did not give rise to liability to customs duties.

The provisions of the Sixth Council Directive 77/388/EEC on the harmonization of the laws of the Member States relating to turnover taxes must be interpreted as meaning that the unlawful importation of counterfeit money into a Member State is not subject to value-added tax.'