

TAX ADMINISTRATION VS. TAXPAYER. A NEW DEAL?

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The evolution of the relationship between the Tax Administration and the taxpayer. From a concept based on tax power, governed by principles and legal rules, to the enhanced relationship based on a fair-play attitude implemented by soft-law instruments.

I.THE ORIGINAL CONCEPT

1.A Public Law concept: a relationship based on the content and exercise of tax power

The concept of tax relationship has its origins in the Public Law doctrine in Germany in the 19th century. The concept of *Gewaltverhältnis* is based on the idea of a relationship focused on the **exercise of tax power**. According to O. Mayer the idea that paying taxes is an obligation created by public authorities is essential. The power to tax is legitimated by law and thus governed by the **principle of legality**, although it is well known that the origin of this principle comes from much earlier times and derives from the old “**no taxation without representation**”.

In order to implement this power and thus the right of the State to levy taxes, the law provides the Tax Administration with the so called administrative powers which, according to most authors, can also be considered part of the power to tax in the broad sense of this concept. These administrative powers are exercised over the taxpayer who, in addition to having the main obligation of paying tax, must fulfill formal duties, most of which concern collaboration with the Tax Administration in the different procedures carried out in order to apply tax law. O. Bühler argued that it is impossible to consider that the parties in the tax relationship are on an equal footing because the State has a superior position to that of a creditor in a private law obligation, and in administrative procedures the powers granted to the Tax Administration make its superiority even more evident.

The German doctrine also had an influence in Italy where authors like Rannelletti or Ricca Salerno shared the view of a tax relationship based on the tax power conferred on the Tax Administration and the taxpayer's submission to that power. In brief, in this relationship, the creditor is the State, which is granted the power to tax and is, therefore, a *potentior persona*.

That was the framework of the relationship between the Tax Administration and the taxpayer in its original dogmatic approach, considered from a Public Law perspective, in other words focused on the Tax Administration's position as a *potentior persona*. The

obvious result was a relationship characterized by the fact that the parties involved were on an unequal footing.

2.A Private Law concept: towards a more balanced relationship (creditor vs.debtor)

The reaction against the above mentioned theory was based on a private law concept: obligation, that is to say, the nexus between creditor and debtor. The idea was to find a suitable concept in order to guarantee that the parties involved in the relationship were on an equal footing (had the same rights and conditions) and this was granted in that the nexus, which is the core of the relationship, has the same structure irrespective of the parties' condition. In other words, as regards the tax obligation, the State is neither more nor less than a creditor, with the same status as any creditor in a private law obligation.

In Germany, the legal doctrine (Hensel, Blumenstein, Nawiasky) considered that the State was subject to the law on an equal footing to that of individuals and from this perspective, the private law concept of obligation represents the legal connection between two subjects who, with the same rights and conditions, defend their contradictory interests.

A similar approach was proposed by the Italian doctrine with the concept "*Il rapporto giuridico d'imposta*" developed by authors like A.D. Giannini and A. Berliri. In brief, the idea was the following:

the tax legislation enacts mutual rights and obligations for the State and for taxpayers which are the content of a special relationship (the tax relationship); thus this content is broad and complex consisting of a central core (the tax obligation, the creditor-debtor nexus) and also different administrative powers, formal duties and rights. This approach also had an influence on the Spanish legal doctrine at that time and inspired the General Tax Act 1963. In the further development of the legal doctrine both in Italy and Spain, this approach was criticised by some scholars who proposed a concept of the tax relationship more focused on procedural aspects and so more public law oriented.

In my opinion, the approach based on the equivalence of tax obligation and private law obligation was the weakest point of this doctrine. It was a purely theoretical approach which did not explain why the tax provisions and, more precisely, those governing tax procedures put the parties involved in the tax relationship on an unequal footing. In my view, the reason is the **principle of legality**, in the sense that the law is the source of the tax obligation (*obligatio ex lege*) and this is the main difference with most private law obligations, in which the source is a mutual agreement (a contract), that is to say the will of the parties. By contrast, the tax obligation is not ruled by the will of the parties, but by the will of the law. This difference is indeed relevant in order to explain not only the content of the creditor's and debtor's positions but also the role played by the Tax Administration, as well as the implementation of these positions through administrative procedures. In this framework, the

Tax Administration exercises its powers in the interest of the law which, in this case, means in the public interest of levying taxes, and on the other hand, the taxpayer makes a compulsory contribution to the financing of public expenditures.

Nevertheless, this approach can be compatible with the aim of creating a more level playing field for the Tax Administration and the taxpayers. But in this case, not only at the theoretical level but also, and above all, in the field of legislation and jurisprudence, the issue is the reinforcement of the taxpayer's position *vis-à-vis* the administrative powers. And this has been the roadmap followed by the further evolution of the tax relationship as we will see next.

II. FURTHER DEVELOPMENTS

1.Reinforcing the taxpayer's position. The defence of taxpayers' fundamental rights

In the past century, more or less since the 80's, a kind of "counterattack" took place in order to put the parties involved in the tax relationship on a more equal footing. The key point consisted in **considering the taxpayer as a citizen entitled to certain rights that must be guaranteed and, therefore, respected by the Tax Administration when applying its administrative powers.**

In brief, this idea reflects the need to find a balance between the citizens' compulsory contribution and the protection of their

fundamental rights, thus determining to what extent there is a limit on both their obligation and their rights. The battlefield was the tax procedure (especially the audit procedure) and the fight centered on application and interpretation of the tax law. This circumstance explains the leading role of court decisions, although changes in tax legislation were also significant.

Precisely on this subject, in 1990 the OECD's Committee of Fiscal Affairs (Working Party number 8) published the document "Taxpayers' rights and obligations. A survey of the legal situation in OECD countries" that, based on country replies to a questionnaire sent out in 1988, was approved by the OECD Council on 27 April 1990. The result of the survey showed that many countries had listed the basic rights and obligations in a **taxpayers' charter**, which in some cases was rather detailed and in other cases in the form of a general statement of the broad principles that should govern the relationship between the tax authorities and the taxpayer. However, with or without a formal taxpayers' charter, the OECD considered that countries may attach equal importance to taxpayers' rights.

As a result of the 1990 survey, the OECD document noted the following rights: the right to be informed, assisted and heard, the right of appeal, the right to pay no more than the correct amount of tax, the right to certainty, the right to privacy and the right to confidentiality and secrecy. With respect to taxpayers' obligations, the document noted the following: the obligation to be honest, the obligation to be co-operative, the obligation to provide accurate

information and documents on time, the obligation to keep records and the obligation to pay taxes on time.

The idea of a taxpayers' charter is important because it means a change of climate, tending to reinforce the taxpayer's position. Just as an example, I can mention that in Spain a specific Act on this topic (*Ley de Derechos y Garantías de los Contribuyentes*) was passed in 1998; these provisions were later included in the current General Tax Act (*Ley General Tributaria*) in force since 2004. Nevertheless in my view, the need for a taxpayer's charter may be a controversial issue since in States governed by the rule of law, **the taxpayer should be considered neither more nor less than a citizen and as such, entitled to fundamental rights that, precisely due to their nature, imply a limitation on the power of the State, which cannot be considered different or superior simply because this power is exercised by the Tax Administration.**

The conflict between the obligation to pay tax and fundamental rights is not exclusive to one single country, but a global problem, although more clearly apparent in the tax law systems of developed countries. As already mentioned, the role of the jurisprudence has been to some extent decisive in reinforcing the taxpayers' position; most of it, obviously, at the national level through decisions of ordinary Courts and especially of Constitutional Courts. At the European Union level, the Court of Justice has set out a relevant doctrine (especially in VAT cases) in order to guarantee the

effectiveness of taxpayers' rights, as well as to adapt the exercise of the Tax Administration's powers to the principle of proportionality.

At this point however, I would like to comment on the doctrine of the European Court of Human Rights (ECHR) in tax matters, which has also attracted the attention of scholars. This jurisprudence deals with the application of the European Convention on Human Rights. This Convention applies in the European Union by express decision of the Treaty, although the EU Charter of Fundamental Rights (2007/C 303/01) should also to be taken into account.

According to the ECHR jurisprudence, the rights protected in article 6 of the Convention can be invoked in the case of tax proceedings, especially when dealing with tax penalties and tax claims. To some extent, it can be said that taxation came into this provision through the back door of the fight against fraud and the increasing criminalization of tax procedures. Implementing article 6 of the Convention implied, in principle, a clear boundary between ordinary tax procedures (assessment, audit, collection) and tax penalties, but the Court disregarded this distinction in cases where resolution of a single procedure (tax audit) could, at the same time, declare the amount both of the tax debt and of the tax penalty.

A relevant example of this was the ECHR's decisions in the *Funke* and *Bendenoun* cases, declaring that the right to remain silent could be invoked by the taxpayer. The debate on this question was, at that time, particularly intense in Spain because the

Constitutional Court (decision 176/1990) held the opposite view, declaring that the right to remain silent cannot be invoked by the taxpayer to justify his refusal to collaborate with the Tax Administration in an audit procedure, otherwise implementation of the administrative powers and thus levying of taxes would be impossible.

In the United States, the jurisprudence of the Ninth Circuit (*Boyd, Couch, Doe, Fuller* cases), based on the distinction between non-tax crimes and tax crimes, declared that the Fifth Amendment could not be invoked when dealing with tax crimes. In the cases *Brooks vs. Hilton Casinos Inc.* (1992) and *United States vs. Turri* (1994), the Court considered that the Fifth Amendment did not guarantee the right of the taxpayer to refuse to provide the records required by the Tax Administration unless the data could be later used in a non-tax criminal procedure. Nevertheless, it must be noted that this distinction was revised by the US Government, which declared that: “The self-incrimination clause of the Fifth Amendment applies in all instances of prosecution, **whether tax related or not**”.

Article 8 of the Convention dealing with the right to privacy has also been invoked and applied in tax cases. Its second paragraph mentions “interference by the public authority” and this can obviously be applied to the Tax Administration in so far as its powers, especially those dealing with investigation in the audit procedure, may affect taxpayers’ privacy.

Last but not least, the property right envisaged in the First Protocol should be mentioned. In this respect, the Court set out a doctrine based on the principle of proportionality as the way to guarantee a fair balance between the taxpayer's individual right (property) and the general interest (levying taxes), both protected in paragraph 1 and paragraph 2 of article 1 of the Protocol. The Court considered that the tax should not be an "excessive burden" for the taxpayer and has applied this principle in cases concerning the exercise of the Tax Administration's powers.

A final remark about the conflict between the obligation to pay tax and the taxpayers' fundamental rights concerns the content and scope of the **ability to pay principle**. This principle legitimates the obligation to pay tax while at the same time placing a limitation on tax power. Therefore, when the Constitution establishes the taxpayers' obligation to contribute to the financing of public expenditure **according to their ability to pay** (i.e.: article 53 of the Italian Constitution or article 31 of the Spanish Constitution), the Tax Administration's powers are reinforced as long as they are legitimated not only by a formal principle (legality) but furthermore by a substantive principle (ability to pay) which expresses an idea of distributive justice. In fact, the Tax Administration exercises these powers not only in the interest of the law but also in the interest of justice. (In this respect, the Spanish Constitutional Court declared that the obligation to pay tax implied the taxpayer's submission to the Tax Administration, thus invoking the old doctrine of a

relationship based on the primacy of tax power; this decision was severely criticized by academics).

But on the other hand, as mentioned above, it seems obvious that the requirement of levying taxes according to the taxpayer's ability to pay means a limitation on the exercise of tax power. This idea has always been recognized by the legal doctrine and some scholars have even proposed **considering the taxpayers' right to be taxed according to their ability to pay as a fundamental right**. In my view, this is an interesting and challenging approach and indeed a question for debate. The idea, as I said before is, that if when dealing with fundamental rights the taxpayer must be considered no more and no less than a citizen, the right to be taxed according to his/her ability to pay should be granted as a specific right of each citizen in his/her capacity as a taxpayer.

2.Reinforcing the Tax Administration's position

A) Fighting tax avoidance

In the field of Tax Law, tax avoidance is a most relevant topic and to some extent a global issue in that it has a common profile in different countries and Tax Law systems. Nowadays, the so called **aggressive tax planning** has had an increasing influence on the tax relationship. This has provoked a reaction by the tax authorities, both at the legislative level in the form of anti-avoidance provisions and at the procedural level in the form of specific administrative

powers in order to implement these provisions. But furthermore, there is a problem relating to the attitude of the parties involved in the relationship (the Tax Administration and the taxpayer). I am referring to **the lack of mutual trust** which results in a lack of legal certainty.

According to a classical distinction, in Civil Law systems anti-abuse provisions are enacted by law - this is the case of the so called general anti-avoidance rules (GAAR, i.e.: article 42 of the German *Reichsabgabeordnung* or article 15 of the Spanish *Ley General Tributaria*) - whereas in Common Law systems, anti-avoidance rules are the result of general criteria established by the Courts (such as business purpose test, wholly artificial arrangements or sham transactions).

However, nowadays, this distinction is far from being so clear-cut because there are examples of Civil Law countries in which the influence of the jurisprudence on this matter has increased and of Common Law countries that have enacted a GAAR.

An example of the first case is Italy, where the Courts support the so called *interpretazione antielusiva* (anti-avoidance interpretation) according to which, even without a GAAR, the Tax Administration can reject abusive transactions, based on direct application of article 53 of the Constitution (contribution according to the ability to pay principle) and on the anti-abuse doctrine of the EU Court of Justice. Most scholars have expressed a negative opinion

of this jurisprudence that is considered contrary to the principle of legal certainty.

An example of the second case is the GAAR enacted in the United States Internal Revenue Code (IRC 770) according to which: “A transaction shall be treated as having economic substance only if a) the transaction changes in a meaningful way (apart from Federal Income Tax effects) the taxpayer’s economic position, and b) the taxpayer has a substantial purpose (apart from Federal Income Tax effects) for entering into such transactions”.

In addition, most tax legislations envisage specific anti-avoidance rules (SAAR), such as the thin capitalization rule, CFC rules or the valid economic purpose requirement, just to mention a few well known examples that are also relevant in the field of EU Tax Law and International Tax Law.

In the case of Tax Treaties, two questions should be taken into account: first, the SAAR provided in the different provisions of a DTC (such as the L.O.B. clauses) and second, the compatibility of domestic anti-avoidance rules (either general or specific) with the Treaty. As is well known, the OECD has shown great concern about this topic since its Report on “Improper use of the Convention”. A recent example in the version of the MC (July 2010) can be found in the concept of “economic ownership” intended to counteract an abusive use of permanent establishments, or the more recent

reports on tackling aggressive tax planning (2011) and tax arbitrage (2012).

Last but not least, EU Tax Law provides another battlefield against tax avoidance, both by means of specific provisions included in the Directives and the Court of Justice's doctrine on abuse of EU Law, setting out a general principle of **prohibition of abuse of EU Law** and concepts such as **abusive practice** in the field of VAT or, in the case of direct taxation, the valid justification for restriction of fundamental freedoms by domestic anti-avoidance rules implemented in the case of **wholly artificial transactions without an economic purpose other than enjoying a tax benefit**.

As far as our topic is concerned, I would just like to mention **the impact of anti-avoidance rules on the tax relationship** and more precisely, on the parties' attitude within this relationship. As I mentioned earlier, the main effect is a lack of mutual trust that, in most cases, may provoke an inadequate or disproportionate application of an anti-avoidance provision, thus increasing the tax risk and lack of legal certainty.

In my view, this is a common problem in many tax jurisdictions. Just as an example, I will refer to the following case decided by the Spanish *Audiencia Nacional* in its decision of 25 November 2010.

The Non-Residents' Income Tax Act, when implementing the Parent-Subsidiary Directive, establishes that the exemption on

dividends paid by a Spanish subsidiary to its parent in another member State will not apply if more than 50% of the parent company is owned by non-EU residents, unless it shows that it carries on an effective business activity or that it has been incorporated for a valid economic purpose other than to apply the exemption. This is a SAAR which combines two criteria based on a look-through approach and the business purpose test.

In the case at hand, a Dutch parent owned 100% of the Spanish subsidiary; an Austrian company owned 100% of the Dutch company; and a German group owned 9% of the Austrian company, the rest of which was owned by numerous shareholders because it was a company listed on the Stock Exchange.

The Spanish Tax Administration refused the exemption and thus demanded from the Spanish subsidiary the withholding tax on the dividends paid to its Dutch parent, considering that it was impossible to know whether or not the indirect ownership was in the hands of EU residents.

The Court (*Audiencia Nacional*) ruled in favor of the taxpayer and was very critical in its ruling with the attitude of the Tax Administration in this case, arguing that it was contrary to the **principles of proportionality, good faith and legitimate trust**. In the Court's view the Tax Inspector had made disproportionate use of the look through approach, resulting in an interpretation *ad absurdum* of the anti-avoidance provision that was wrong and

unlawful. Moreover, such an interpretation would make it impossible to apply the Directive to listed companies, which was obviously far from being right or logical.

B) Launching cross-border cooperation

As is well known, in the field of International Taxation the principle of residence means that the State of the taxpayer's residence is entitled to levy tax on the taxpayer's worldwide income or capital; so in this case, the tax provisions may apply to tax events that take place outside the territory of that State. However, this extraterritoriality of tax power does not extend to administrative powers, because the Tax Administration cannot exercise its powers beyond the territory of the State to which it belongs.

The territoriality of the Tax Administration's powers is in my view, the Achilles' heel of an international tax system based on the priority of the residence principle and, more precisely, on the aim of taxing worldwide income or capital, because this limitation does not guarantee the effective taxation of tax events produced in the territory of another State, not to mention the influence of this circumstance in the field of international tax fraud; furthermore, this limitation may also be a problem in the case of non-resident taxpayers if the withholding tax instrument does not sufficiently guarantee the effective levying of the tax by the Tax Administration in the State of source.

Recent examples show the reaction of the States which tend to strength the Tax Administration power in order to get information about their taxpayers' assets located abroad. In this respect, I can mention the FATCA provisions enacted in the United States in 2010 according to which, both US taxpayers and foreign financial institutions must report to the IRS information about financial accounts. In Spain, the draft legislation against tax fraud (2012) includes a provision on compulsory information by taxpayers about their assets located abroad. In both examples, the regulations provide severe consequences in case of no compliance.

The international organizations involved in this area as well as the European Union authorities are perfectly aware of this problem and so in recent decades they have launched several initiatives and regulations in order to strengthen the cooperation between the Tax Administrations of different States. In the case of the OECD, the traditional instrument has been the **exchange of information** provision in article 26 of its Model Convention and also, since 2003, article 27 on **mutual assistance in collection of taxes**. As far as exchange of information is concerned, I should also mention the OECD Model Agreement launched in 2002 and the Multilateral Convention on administrative cooperation in tax matters, a joint initiative launched by the OECD and the Council of Europe in Strasbourg on 25 January 1998.

But the most significant regulations in this field have been set out within EU Law. I will just mention the most recent ones currently

in force: the Savings Directive (48/2003) that provides an automatic exchange of information system; Directive 2010/24 on “Mutual assistance for the recovery of claims relating to taxes, duties and other measures”, and Directive 2011/16 on “Administrative cooperation in the field of taxation” (not yet completely implemented by all Member States).

In my view, the last two Directives can be considered a decisive step in solving the problem and to some extent represent an attempt to override national boundaries when implementing administrative powers. Needless to say, if this is the case, tax assistance and cooperation mean an important reinforcement of the Tax Administrations' position, especially *vis-à-vis* their taxpayers. As far as the topic of this conference is concerned, I will outline the following examples which illustrate this reinforcement.

The first example may be found in the Cooperation Directive (2011/16), which provides an instrument that has always been considered most efficient by tax officials: the **automatic exchange of information** (article 8). In principle, this provision will come into force in 2014 and be implemented only for information on salaries, pensions, director's fees, life insurance and immovable property, but could be extended to other types of income as of 2017. Obviously, this approach does not mean that administrative powers are extraterritorial, but it does indeed reinforce their effective exercise.

A second example is provided by the Mutual Assistance Directive (2010/24), which under the principle of **equal treatment** states in article 13 that any claim for recovery coming from the applicant State will be treated as if it was a claim of the requested State. Moreover, a similar effect to the exercise of a cross-border tax power is reached through the **uniform instrument permitting enforcement (UIPE)** regulated in article 12, which can be used not only for enforcement of the tax claim but also for implementing precautionary measures. I said “similar” and not “same” effect as that of a cross-border power because, as provided in article 16, it is not yet the Tax Administration of the applicant State but that of the other State acting in a kind of “substitutive” role that exercises the powers granted through the UIPE.

A third example and maybe the most significant, included in both Directives (article 7 in 2010/24 and article 11 in 2011/16) refers to an **administrative cooperation which allows the effective exercise of the Tax Administration’s powers in the territory of another Member State**. Under the principle of mutual consent, these provisions regulate both the presence and participation of Tax officials of the applicant State in tax procedures carried out in the territory of the requested State. However, the most relevant issue is that these officials are allowed to interview the taxpayer and examine his records and also, under the principle of equal treatment, any refusal or negative reaction of the taxpayer shall be considered as if it took place *vis-à-vis* the Tax officials of the requested State. I dare say that, in this case, reinforcement of the

Tax Administration's position also implies the **cross-border exercise of administrative powers**.

At the end of the day, cooperation and mutual assistance will reinforce **the principle of effectiveness**, because the content of the administrative powers remain the same, but their territorial scope has been enlarged and this circumstance will result (at least, potentially) in a more efficient implementation.

As usual, the evolution of the tax relationship follows a "pendulum motion", because reinforcement of the Tax Administration's position puts the taxpayer in a weaker position. I say nothing new when I say that the negative side of the cooperation and mutual assistance legislation is the lack of protection of the taxpayers involved in these procedures. As far as exchange of information is concerned, this has been the most critical remark expressed by academics and in international forums. Just to mention an example: the General Report by Gangemi in the 44th IFA Congress in Stockholm or the OECD Report on "Tax information exchange between OECD member countries" (1994), which declared that at least some taxpayers' rights such as notification, hearing, intervention and claim should be guaranteed.

A most critical issue related to the taxpayer's position concerns the consequences of these procedures on the statute of limitations. In this respect, article 19.2 of the Mutual Assistance Directive (2010/24) states that, under the principle of equivalence,

the provisions on interruption, suspension or prolonging of the period of limitation in force in the requested Member State will apply.

In my opinion, there may be a risk of uncertainty for the taxpayer if he/she is not aware of the steps and actions carried out by the Tax Administration in a mutual assistance procedure and so counts on the usual period of limitation under the statute of limitations being applicable

Finally, I would like to mention the problems related to **the use of the information** obtained by the Tax Administration, especially in cases of the so-called “transmission by chain” involving several States. The Directives refer to the information obtained through a mutual assistance or exchange of information procedure and do not deal with the origin of the information received by the first Administration involved in the “chain”. However, precisely this has been the relevant problem in very well known cases in recent years, because the information received by a Member State from a third State (Liechtenstein in 2008 or Switzerland in 2010) had been obtained by unlawful means. In this respect, it must be noted that in the case of the information from Switzerland used by the French Tax Administration, the *Cour d'Appelation de Paris* in its decision of 8 February 2011 ruled in favor of the taxpayer, holding that the illicit origin of the information prevents it from being used by an administrative or judicial authority.

III. THE ENHANCED RELATIONSHIP. A NEW DEAL?

1. The enhanced relationship: current developments

As is well known, a new approach to the relationship between the Tax Administration and the taxpayer has been developed, exemplified by the concept of the so called **enhanced relationship (ER)** which, in my opinion is a turning point in the evolution of this relationship for several reasons. First, it does not follow the traditional “pendulum” motion because it does not correspond to a further reinforcement of one of the parties’ position; second, the concept is not related to the legal position (powers, obligations or rights) of the parties, but to their **attitude** in the defense of these positions; third, and precisely because of this concept, the ER is **implemented through soft-law instruments**; and fourth, the idea is not due to a change in legislation, the influence of any Court decisions or a new concept proposed by academics, but to the initiative of International Organizations, mainly the OECD that launched the ER in the Seoul Declaration 2006 and in the Capetown Communication 2008, as a result of the work done at the Tax Administration Forum. I would also like to mention the IFA Initiative on the ER and the growing interest recently shown by academics in this topic.

Earlier in this lecture, I made reference to the **lack of trust** as one of the main problems of the current relationship between the Tax Administration and the taxpayers. I mention this because in my

view **to restore the trust between the parties is precisely the main goal of the ER**. This idea was clearly expressed in a relevant OECD document on this topic (The Tax Intermediaries Study, Working Paper 6). The starting point is the limited scope of the so called basic relationship “characterized by the parties interacting solely by reference to what each is legally required to do without any urging or persuasion from the other”. I would like to underline this idea of going beyond the legal requirements; however, it is not just a question of “one more step forward” but rather a different approach altogether.

Concerning “**the importance of establishing trust**”, this working paper states that the ER requires the parties “to go beyond the bare minimum that they are obliged to do...and they will not do so on a sustained basis **unless trust is established and maintained**” and also that trust “requires each party **to behave** in a way that is seen by the other parties as trustworthy, which means credible, intimate and not self-oriented”. I have emphasized the word “behave” because this is at the heart of the matter: **the ER is about the behaviour** of the Tax Administration, taxpayers (and also tax intermediaries). In this respect it has been said that “legitimate taxation is not only a matter of the law and legal principles, but also of proper treatment” (Gribnau).

But what are the reasons for the need to restore mutual trust in this relationship? Briefly, the main reason is that the lack of trust means uncertainty, and uncertainty increases the risk - in this case,

the tax risk both for the Tax Administration and for the taxpayer. The idea is as simple as this and illustrates the background of the ER. In the case of the Tax Administration, efficiency when dealing with tax risk management requires trustworthy information to be provided by the taxpayer and for this a new framework is necessary based on transparency, proportionality and an attitude that is not self-oriented, on a *quid pro quo* basis. The same can be said for the taxpayer, especially in the case of companies and risky decisions such as those related to aggressive tax planning in that tax risk management has to do with corporate governance. To summarize: we are talking about **a relationship based on fair play**; this is the new playing field and the essential rule of the game.

The question now is: what legal principles - if any - govern the ER. At first sight, it could be argued that law is primarily to do with facts and not with attitudes and, therefore, the aim of restoring the trust between the parties would not be backed by any legal principle. But in my view, this conclusion is not correct, because the lack of trust reflects a lack of legal certainty which is obviously a legal principle. So the idea of the ER is, at least indirectly, based on the **principle of legal certainty** and also on the **principle of efficiency** of the Administration (which for example, in Spain, is enshrined in the Constitution), not to mention other principles such as proportionality reflected in the content of the ER, as we will see next.

According to WP 6 mentioned above, the ER “is not an end in itself but a means of establishing the right amount of tax payable by

taxpayers in a quick, fair and efficient manner”. So the proposal identifies the concept as an instrument constructed, as I said before, on a *quid pro quo* basis, thus requiring **reciprocity** in the change of attitude, that is, on the part of both the Tax Administration and the taxpayers (including their tax advisers). Therefore, the content of the ER is described through the requirements proposed for the parties, which are essentially the following:

For taxpayers and advisers: **full and timely disclosure and transparency**, which involves giving voluntary information about potential tax risk positions (referred to as a kind of “self-risk assessment” in the ER) and providing comprehensive responses to the tax authority.

For the Tax Administration: First, commercial awareness (understanding of the taxpayer’s commercial and tax strategy). Second, an impartial approach (acting fairly and not mainly revenue-oriented). Third, proportionality (in this case understood as a kind of flexibility, because “there is often no single, right amount of tax, and the Tax Administration should determine the one which is acceptable for the revenue body”). Fourth, disclosure and transparency (in reciprocity with the same requirement for the taxpayer, in this case including motivation and not using privileges to avoid disclosure). The fulfillment of these four requirements should lead to **responsiveness** and thus contribute to **tax certainty**.

Last but not least, there is a significant difference between **implementation of the ER** and the usual way of implementing the relationship between the Tax Administration and the taxpayer. In principle, this implementation should not need any significant change in the legislation. Due to the special characteristic of the ER which is that, as I pointed out before, it is to do with the attitudes and behaviour of the parties rather than with their legal positions, it has been considered that the most suitable way to implement it is through **soft-law instruments**.

Scholars have provided a wide range of definitions of soft-law, all of which are very similar. The common standard considers soft-law as instruments that are not legally binding but relevant in that they try to influence future legislation, interpretation of current laws or conventions, or the behaviour of States. This is a broad concept which includes different types of instruments such as recommendations, guidelines and commentaries, standards or codes of conduct.

In the case of the ER, WP 6 suggests different alternatives, such as: a charter (setting out the minimum requirements for compliant behaviour), a unilateral declaration by the revenue body, or an informal agreement between the parties. Some examples of these alternatives can be found in the experiences in certain jurisdictions, especially those who have implemented disclosure rules or cooperative compliance, such as: Australia, Ireland, Italy,

the Netherlands, New Zealand, Spain, the United Kingdom and the United States.

To go into this issue in more detail I have chosen as an example the **Code of Best Tax Practices** set out by the Spanish Tax Administration (*Agencia Tributaria*) in July 2011. In this case, the ER is implemented through a dual process: first, the Code in itself (a code of conduct) is a unilateral declaration by the Tax Administration; second, every taxpayer (in this case, large companies), **on a voluntary basis**, signs an agreement with the *Agencia Tributaria* so both parties agree to comply with the requirements of the Code. I remark the word “voluntary” because, for instance, the Spanish Code does not set out mandatory disclosure rules, which is a common experience in some other countries.

The Spanish Code was a result of the Large Businesses Forum and identifies three groups of best tax practices, described in the usual *quid pro quo* format, characteristic of the ER. The first group deals with requirements for taxpayers regarding transparency, good faith and cooperation with the Tax Agency in company tax practice, detailed in practices such as: avoiding the use of structures of an opaque nature, collaborating in the detection and solution of fraudulent tax practices or the person responsible for tax affairs reporting to the board of directors on the tax policy of the company. The second group deals with requirements for the Tax Administration concerning transparency and legal certainty in the

application and interpretation of tax regulations by the Tax Agency, detailed in practices such as: coherence of the criteria for interpretation; setting up adequate procedures for the tax treatment of certain transactions, allowing the taxpayer to file together with his tax return a form explaining the facts and criteria applied so that if these are reasonable they can be taken into account; and guaranteeing the full exercise of taxpayers' rights. The third group refers to conflict avoidance and reducing the number of lawsuits since this should be the logical effect of a relationship based on mutual trust. For this purpose, the Code refers to several practices, most of them related to the audit procedure, and encourages agreements in different steps of this procedure.

2. Critical remarks

As far as the topic of this lecture is concerned, the main question arising from the ER is: Are we actually facing a new deal? In my opinion, for the time being it may be too soon to give the right answer to this question. Two possible alternatives can be debated:

The first is a positive view: The ER has an ambitious goal and implies a complete, in-depth change in the tax relationship. Although the legal positions of both parties have not changed that much and the principles were already there, the aim of the ER consisting mainly in restoring the mutual trust (and thus reinforcing legal certainty) is worthwhile. The *quid pro quo* approach puts an end to the pendulum swing of this relationship. Implementation through

soft-law instruments is coherent with the aim of the ER and within this framework not only legal certainty but also the principle of effectiveness could be the winners of the game.

The second is a negative or, at least, skeptical view: The aim of the ER is actually not as ambitious as it seems to be. “To restore the mutual trust” sounds good, but the hidden, underlying goal, in fact, the real reason behind the launching of the ER is the need to solve the problems created by aggressive tax planning. But, if this is the case, the question is: will the *quid pro quo* approach really work? Who needs whom more?, not to mention the most extended criticism of the concrete experiences dealing with the ER in some jurisdictions (also of course in the case of the Spanish Code) concerning the discrimination of SMEs and individual taxpayers since so far the ER has only been implemented in the case of large companies.

I would just like to make one final remark, which has much to do with this forum (an association of Tax Law Professors). The question concerns the role of academics in the evolution described above. If we go back to the first point of this lecture, we can see the leading role played by the legal doctrine in the different proposals for a dogmatic approach to the concept of tax relationship. In the further evolution, focused on the reinforcement of the parties, the leading role was played by the Courts and the legislator, whereas the role of academics was mainly limited to analysis, criticism and debate of those decisions. Now, what about the ER? In this case, the leading

role is being played by International organizations launching the initiative and by the parties (Tax Administrations and large companies), implementing soft-law instruments. What is our role – if any – in this context? I leave the question open and suggest dealing with it as an academic topic for a future Congress.