

TAX AVOIDANCE AND RATIONALITY OF LAW

Hanna Filipczyk

MONOGRAFIE



Wolters Kluwer

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“Contravenes the law whoever does what the law forbids,
but acts fraudulently who without infringing
the wording of the law, circumvents its sense” (Paulus)¹

“There is neither logic nor morality in tax law,
just a bunch of rules” (anonymous tax scheme inventor)²

¹ “Contra legem facit, qui id facit, quod lex prohibet, in fraudem vero qui, salvis verbis legis, sententiam eius circumvenit” (*Corpus iuris civilis*, Dig. 1.3.29).

² Words of a tax scheme inventor interviewed (cited in: J. Braithwaite, *Markets in Vice, Markets in Virtue*, Oxford University Press, Oxford 2005, p. 58).

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ABBREVIATIONS AND ACRONYMS

- ATA Directive** – Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, OJ L 193, 19.7.2016, pp. 1-14
- Directive 2009/133** – Council Directive 2009/133/EC of 19 October 2009 on the common system of taxation applicable to mergers, divisions, partial divisions, transfers of assets and exchanges of shares concerning companies of different Member States and to the transfer of the registered office of an SE or SCE between Member States, OJ L 310, 25.11.2009, pp. 34-46
- Directive 2011/96** – Council Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States, OJ L 345, 29.12.2011, pp. 8-16
- Directive 2015/2376** – Council Directive (EU) 2015/2376 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation, OJ L 332, 18.12.2015, pp. 1-10
- Directive 2016/881** – Council Directive (EU) 2016/881 of 25 May 2016 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation, OJ L 146, 3.6.2016, pp. 8-21
- Proposal for the CCCTB Directive** – Proposal for a Council Directive on a Common Consolidated Corporate Tax Base (CCCTB), Strasbourg 25.10.2016, COM(2016) 683 final
- Proposal for the CCTB Directive** – Proposal for a Council Directive on a Common Corporate Tax Base, Strasbourg 25.10.2016, COM(2016) 685 final

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| Proposal for the Mandatory Disclosure Directive | - Proposal for a Council Directive amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements, Brussels 21.6.2017, COM(2017) 335 final |
| Recommendation of 6.12.12 | - Commission Recommendation of 6.12.2012 on aggressive tax planning, Brussels 6.12.2012, C(2012) 8806 final |
| Recommendation on Tax Treaty Abuse | - Commission Recommendation on the implementation of measures against tax treaty abuse, Brussels 28.1.2016, C(2016) 271 final |
| VCLT | - Vienna Convention on the Law of Treaties (with Annex) concluded in Vienna on 23 May 1969 |

* * *

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| ATP | - aggressive tax planning |
| BEPS project | - Base Erosion and Profit Shifting project |
| CC | - co-operative compliance |
| CFC | - controlled foreign corporation |
| CJEU | - Court of Justice of the European Union |
| CSR | - corporate social responsibility |
| FTA | - Forum on Tax Administration |
| GAAR | - general anti-avoidance rule |
| IFA | - International Fiscal Association |
| LOB | - limitation on benefits |
| MNE | - multinational enterprise |
| OECD | - Organisation for Economic Co-operation and Development |
| PBL | - principle-based legislation |
| PE | - permanent establishment |
| PPT | - principal purpose test |
| SAAR | - specific anti-avoidance rule |
| STAAR | - specific targeted anti-avoidance rule |
| TAAR | - targeted anti-avoidance rule |

FOREWORD

“Tax avoidance is a taxpayer’s course of action in line with the letter but contrary to the spirit of the law”. Definitions phrased along these lines can be found in many policy statements and legal provisions. “Fiscal” and “moral termites” (in the words of Vito Tanzi¹ and John Braithwaite²) are eating away taxes due, not only by tax evasion but by a more sophisticated conduct as well: by tax avoidance. I undertook this theoretical journey to understand this phenomenon.

The National Science Centre in Poland funded the research and publication of this book (research project no. 2014/15/D/HS5/01599). Financial support from this institution is gratefully acknowledged.

My research stay at the Max Planck Institute for Tax Law and Public Finance in Munich in October 2016 made my work progress immensely. I am grateful to Professor Wolfgang Schön for hospitality and for providing me with the opportunity to use vast resources of the Institute’s library and to exchange views with academics there.

Of special note is the gratifying acquaintance I made of Professors John Prebble and Hugh Ault. I benefitted a lot from the seminar on “Jurisprudential Perspectives on Taxation Law” taught by Professor Prebble at the Vienna University of Economics and Business in September 2015. Professor Ault was my mentor in writing an article within

¹ V. Tanzi, *Globalization, Technological Developments, and the Work of Fiscal Termites*, Washington DC, International Monetary Fund WP/00/181, November 2000, *passim*.

² J. Braithwaite, *Markets in...*, p. 14.

the scope of this research project (under the auspices of the IBFD) in January-May 2016. I do not have words to express how kind and encouraging both Professors have been to me. Meeting them was a true honour and pleasure.

The partial results of the project leading to this book have been presented at conferences in Munich, Nuremberg, Vadstena, London, Amsterdam, Warsaw, Łódź, Zamość and Zakopane. I am indebted to the participants of these events for their numerous valuable contributions.

My gratitude also goes to the editorial team of Wolters Kluwer. If asked by a colleague where to publish, I unhesitatingly point to them as *the place*.

And let me thank only in person to the one without whom my life would be dull and senseless.

Chapter I

INTRODUCTION

1. Purpose of the study

This book, and the research project the results of which it summarizes, sets out to answer the questions of *what* tax avoidance essentially is, and *why* and *how* (by what legal instruments) it should be countered. So outlined, the topic would be incredibly – and excessively – vast. It is narrowed down by the specific outlook of the project. Tax avoidance is conceived of as a practice defeating rationality of law. This was the key used to investigate problems dictated by the topic of the study.

For the purposes of the project “countering tax avoidance” is understood as undertaking actions (taking measures) within the operative legal interpretation (i.e. interpretation performed in the process of law application) and law-making which are preventive, reparative or repressive in nature, i.e. which aim, respectively, to prevent tax avoidance (including deterring it), to reverse its negative consequences or to sanction it. The ultimate goal of these actions is to eliminate altogether or (more realistically) to minimise the scope of tax avoidance and its adverse consequences, including but not limited to, negative effects for state revenues.

In the project the following research hypotheses were subject to verification:

- 1/ Tax avoidance is a taxpayer’s action resulting in tax consequences which are in line with the letter of the tax law but contrary to the rationality of law (to its spirit).

-
- 2/ The lawmaker should counter tax avoidance.
 - 3/ An important reason why the lawmaker should counter tax avoidance is that the latter defeats the rationality of law.
 - 4/ Counteracting tax avoidance does not contradict the rule of law principle.
 - 5/ Effective and fair counteracting of tax avoidance requires substantive tax law to have appropriate characteristics, i.e. to be such that it can be rationalised.
 - 6/ Effective and fair counteracting of tax avoidance requires also enacting provisions directly oriented towards this goal (i.e. anti-abusive) which provide legal grounds to imperative and non-imperative actions of tax administration authorities.
 - 7/ The lawmaker should enact a general anti-avoidance rule-clause (GAAR), as an important regulation counteracting tax avoidance, providing legal grounds to imperative actions of tax administration.
 - 8/ The lawmaker should enact the legal framework for a cooperative compliance programme, as an important regulation counteracting tax avoidance, giving legal grounds to non-imperative actions of tax administration.

The book is organized in accordance with these research hypotheses.

The analysis is universal in scope: for the most part it concerns all taxes. At the same time, the considerations are made with special focus on corporate income tax. One chapter is dedicated specifically to this tax. This is explained by the fact that currently income tax is the most prone to tax avoidance. It is this type of tax avoidance that is the most widespread and poses the most significant challenge to law and public finance, in terms of both its financial impact and difficulty to handle it. It is thus a good illustrative example: a case enabling to show what is, and what is not, achievable by means of the proposed conception of tax avoidance.

2. State of the art

Tax avoidance, resulting in particular in the tax base erosion in corporate income taxation, is indisputably an important problem of present-day law, economy and social life. The initiatives aiming to counteract it are undertaken globally, in particular through the G20/OECD Base Erosion and Profit Shifting project (“the BEPS project”)¹, at the level of the European Union, in particular in the EU Anti-Tax Avoidance Package², as well as domestically.

These actions, numerous and determined, but often improvised *ad hoc* and reactive, are accompanied by scientific reflection. Literature on the subject of tax avoidance is extensive and ever-growing. In particular, there is immense literature focused on technical aspects of anti-avoidance legal measures. The areas covered include:

- abuse of the EU law, including the analysis of the jurisprudence of the Court of Justice of the European Union (the CJEU);³
- comparative analysis of domestic anti-avoidance judicial doctrines and statutory provisions, focusing in particular on general anti-avoidance rules (GAARs);⁴

¹ The project was undertaken by the OECD at a request of the G20 leaders on the basis of the BEPS Action Plan delivered in July 2013 and formally endorsed by the G20 leaders in the St Petersburg Declaration of September 2013. The final package of measures (summarised in 15 reports on respective so-called “Actions”) was delivered in October 2015. It is now in the implementation phase.

² The Anti-Tax Avoidance Package announced by the European Commission on 28 January 2016. It is structured around the ATA Directive, Recommendation on Tax Treaty Abuse, Directive 2016/881, Communication from the Commission to the European Parliament and the Council on an External Strategy for Effective Taxation, Brussels, 28.1.2016, COM(2016) 24 final, and, recently, the Proposal for the CCTB Directive and the Proposal for the CCCTB Directive. It is a response to the challenges addressed by the BEPS Project, as well as to the BEPS Project itself (the aim of the Package is to prevent a fragmentation of the internal market resulting from “uncoordinated unilateral actions by member states” following the OECD BEPS outcomes; see Communication from the Commission to the European Parliament and the Council: *Anti-Tax Avoidance Package: Next steps towards delivering effective taxation and greater tax transparency in the EU*, Brussels 28.1.2016, COM(2016) 23 final).

³ See, *ex multis*, R. de la Feria, S. Vogenauer (eds.), *Prohibition of Abuse of Law: A New General Principle of EU Law*, Hart Publishing, Oxford/Portland 2011.

⁴ See, e.g. R.A. Tooma, *Legislating Against Tax Avoidance*, IBFD, Amsterdam 2008; K.B. Brown (ed.), *A Comparative Look at Regulation of Corporate Tax Avoidance*, Springer,

BIBLIOTEKA PRZEGŁĄDU PODATKOWEGO

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“Fiscal” and “moral termites” (in the words of Vito Tanzi and John Braithwaite) are eating away taxes due, not only by tax evasion but also by a more sophisticated conduct: tax avoidance. *Tax Avoidance and Rationality of Law* is a theoretical journey undertaken to understand this phenomenon.

It is a bold and inspiring study of tax avoidance, leading through the questions of what tax avoidance essentially is, and why and how (by means of what legal instruments) it should be countered. The central insight of the publication is that tax avoidance defeats rationality of law – violates law-as-rationalised – and that this is the exact reason why it is wrong and it should be combated.

The book contributes to a lively contemporary debate on legal and ethical aspects of tax avoidance. By explaining its nature and re-examining well-known objections against anti-avoidance measures, the publication legitimises current initiatives such as the OECD/G20 Base Erosion and Profit Shifting (BEPS) project or national general anti-avoidance rules (GAARs). It also postulates the enrichment of the typical toolbox employed to prevent and counteract this phenomenon with principle-based legislation and co-operative compliance programmes.

The book is aimed at attracting a wide readership, including tax academics and tax judges.



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