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Some Recent Tax Decisions of the European Court of Human Rights

This article examines some recent cases of the European Court of Human Rights concerning, in particular, allocation of taxpayer individual identification numbers, the right to a fair trial and retrospective tax legislation (and disproportionate penalties).

1. Sinful Taxpayer Identification Numbers

Tax cases that raise an alleged infringement of Art. 9 of the European Convention (the freedom of religion) are rare. In *Tamara Skugar & Others v. Russia*,[1] three Russian ladies alleged that the allocation to them of taxpayer individual identification numbers (which consisted of a 12-digit sequence) infringed their rights to religious observance because giving numbers to people was a forerunner of the mark of the antichrist.[2]

In fact, the Russian Orthodox Church had adopted a position that the use of taxpayers' identification numbers was not contrary to religious practice, and the Russian revenue service had made it clear that a taxpayer who objected to the use of a number could correspond with the service using their normal personal details and not the number.

Not surprisingly, the European Court of Human Rights (ECtHR) held that the use of taxpayer identification numbers did not infringe Art. 9: "the method or organisation of the State taxation database involving the use of individual taxpayers' numbers did not amount to an interference with the applicants' right to freedom of religion under Article 9 of the Convention". This is in line with case law such as *C v. United Kingdom*[3] which held, in the context of Quakers who objected to their taxes being used in part to pay for military expenditure, that there was no breach of Art. 9.

2. The Scope of Art. 6

Issues continue to arise concerning the scope of Art. 6 of the European Convention (the right to a fair trial). In *Niedzwiecki v. Germany (No. 2)*[4] the applicant was a Polish national living in Germany who had been denied child benefits on the grounds that he did not have full residence in Germany. The applicant's claim for child benefit went back to July 1995. Following a reform of the law on child benefits, the relevant legislation was enacted as part of the Income Tax Act with effect from 1 January 1996. The applicant wished to complain that the length of proceedings to dispute the refusal of child benefit had infringed the requirement in Art. 6 for a determination within a reasonable time. In order to be able to rely on Art. 6, he had to show his claim fell within the scope of that Article.

The German government argued that Art. 6 was not applicable to tax proceedings, that child benefits were granted on the basis of the Income Tax Act, and that when an applicant applied for child benefit the tax authorities – when assessing income tax for a year – might conclude that a child-related tax exemption was more advantageous than the child benefit and grant that tax exemption instead. The German government relied, of course, on the decision in *Ferrazzini v. Italy*[5] that tax disputes fall outside the scope of civil rights and obligations.

In this case, however, the ECtHR concluded that it was not convinced that the issue was a tax matter falling outside the scope of Art. 6. Child benefits were social benefits, at least as long as the tax exemption was not found to be more advantageous to the taxpayer. Proceedings concerning child benefits are not excluded from the scope of Art. 6. The Court then went on to conclude that the reasonable time requirement in Art. 6 had been breached.

While the jurisprudence of the ECtHR has come to deny that ordinary tax disputes fall within the civil scope of Art. 6, the Court has been willing to extend the scope of "criminal charge" to apply to more and more tax penalty cases. This is illustrated by the decision in *Impar Limited v. Lithuania*.[6] Following a tax audit, the Vilnius City tax authorities concluded that the applicant company's book-keeping was fraudulent and imposed a fine which was subsequently reduced to 5% of the company's annual income. The company disputed the additional tax and the penalty: the proceedings lasted more than six years. The company wished to complain of the length of the proceedings: the ECtHR held that tax disputes generally fall outside the scope of Art. 6, but that the fine for persistent tax law violations of 5% was both deterrent and punitive so that the company was charged with a criminal offence. The proceedings, therefore, fell within the scope of Art. 6; bearing in mind a two-year delay while an expert report was prepared, a period of more than six

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1. Application No. 40010/04, Decision of 3 December 2009.
2. See Revelations, Chapter 13 v. 15-16.
3. Application No. 10358/83, Commissioner Decision of 15 December 1983.
4. Application No. 12852/08, Decision of 1 April 2010.
5. Application No. 44759/98.
6. Application No. 13102/04, Decision of 5 January 2010.

years for the proceedings to go through three levels of jurisdiction exceeded the reasonable time requirement.

Thus, disputes which may run into millions of euros but concern only the quantum of liability to tax do not come within Art. 6, while tax penalties of 5% or above benefit from the criminal protections in Art. 6. It really is time for the ECtHR to review where its jurisprudence has led it to in the area of tax proceedings.

3. Retrospective Tax Legislation; and Disproportionate Penalties

On 15 March 1983, the local Italian municipality resolved to compulsorily acquire some land from the original applicant in the case of *Belmonte v. Italy*.[7] The original applicant (he had died by the time of the judgment of the ECtHR) brought an action seeking compensation for the expropriation, which was awarded in February 1990 and became finally binding on 8 May 1991. There were many delays by the local municipality in paying this compensation: an initial tranche was paid on 27 May 1992 with the final tranche being paid on 4 January 1995. This final tranche was subject to a 20% retention at source in accordance with new legislation which came into force on 30 December 1991 – prior to that date, no withholding at source applied to similar compensation.

The applicant complained of a breach of Art. 1 of the First Protocol of the European Convention (right to enjoyment of possessions) on the grounds that the legislation was operated retrospectively to an award of compensation that had become final before the imposition of the withholding tax. In particular, he complained that the delay on the part of the municipality in paying the compensation had resulted in the payment taking place after the new legislation came into force. The Italian Court of Cassation rejected the applicant's claim on the grounds that the legislation applied in relation to the time when the payment was made and not when the property was acquired by requisition.

The ECtHR was more sympathetic to the applicant. Taxation is an exception to the right to enjoyment of possessions in Art. 1 of the First Protocol, and may contravene that right if the tax imposed is an excessive charge or fundamentally undermines the financial situation of the taxpayer. The imposition of the 20% withholding tax on compensation was within the margin of appreciation of the State, and the Court confirmed that as a matter of general principle Art. 1 of the First Protocol does not prohibit retrospective tax legislation.[8]

However, it was necessary to consider the applicant's claim in the light of the particular facts, particularly the delay on the part of the municipality in paying the compensation: had the municipality paid punctually, then it would have preceded the introduction of the withholding tax. In the light of those particular facts, the application of the withholding tax in this case failed to meet the fair balance between the general interests of the public and the need to safeguard the fundamental rights of the individual. The case confirms, therefore, the general principle that Art. 1 of the First Protocol does not prohibit retrospective tax legislation, but that in individual cases retrospective legislation may impose an excessive burden on the individual and breach that individual's rights.

Art. 1 of the First Protocol is also relevant to the determination of whether penalties in tax matters are disproportionate or not. However, there has been little case law on this area.[9] In the case of *Monedero & Others v. France*,[10] the issue was whether cumulative fines were disproportionate. Between 1999 and 2005 the applicants (husband and wife) owned some buildings which were used to run an unlicensed gambling activity called "rifles". Following a raid by Customs agents, the applicants confirmed that they had a turnover from the games in excess of EUR 1.2 million over a number of years, but the company that operated the games had only made a profit of around EUR 3,000 and they personally had only received around EUR 34,000 as income and dividends related to the activity. The applicants also declared that their total assets equalled approximately EUR 800,000.

Nevertheless, the applicants were condemned to pay an amount of duties evaded, together with three penalties, each one equal to the amount of duties evaded. Even following a reduction on appeal, they were subjected to total payment of duties and penalties exceeding EUR 2.7 million. They argued that the penalties were disproportionate.

The ECtHR confirmed that a penalty could exceed the margin of appreciation enjoyed by a State if it imposed an excessive charge on the individual or fundamentally undermined the individual's financial situation. However, very surprisingly, the Court found no breach in this case. The legislation was concerned with games of chance and there was a public interest in regulating such games. The applicants had operated an unauthorized gaming activity in order to make a profit and had tried, for example, to interfere with witnesses. The ECtHR considered that the penalties came within the wide margin of appreciation enjoyed by the State in tax matters, particularly given the public interest in combating money laundering. In the particular circumstances, the Court concluded that the imposition of the sanctions was not disproportionate.

Amongst other things, these two cases illustrate that the test of proportionality can become highly subjective, the ECtHR finding the measures disproportionate in one case but proportionate in another. The *Monedero* case must be seen as turning on its special facts related to control of illegal gambling. As the fines imposed exceeded by more than three times the property owned

7. Application No. 72638/01, Decision of 16 March 2010 – currently only available in French.
8. The ECtHR cited the decision in *MA v. Finland* (Application No. 27793/95, Decision of 10 June 2003).
9. One of the few relevant cases being the case of *Mamidakis v. Greece* (Application No. 35533/04, Decision of 11 January 2007).
10. Application No. 32798/06, Decision of 2 February 2010.

by the applicants it is very hard to see how that level of fine would not have undermined the economic viability of the applicants.

4. And for Those with Three and a Half Hours to Spare

The ECtHR has now held its public hearing in the *Yukos* case[11] on 4 March 2010. The entire public hearing can be viewed on a webcast, the hearing lasting for an unusually long three and a half hours. For those who wish to view this, go to the welcome page for the ECtHR and the webcasts can be found under the heading "webcasts of hearings".[12] A judgment in the case is not expected for some months.

11. Application No. 14902/04.
12. See http://www.echr.coe.int/ECHR/EN/Header/Press/Multimedia/Webcasts+of+public+hearings/.