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The Involvement of the Taxpayer in the Public Administration Decision

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Abstract

The relationship between taxpayers and Tax Authority and the involvement of the taxpayer in the public administration decision is a very important area of investigation in Italian tax law. This relationship is based on equity and cooperation in good faith, which stems from constitutional principles, such as the principle of sound administration (Art. 97 Italian Constitution), fairness and solidarity (Art. 3 Italian Constitution). Therefore, Tax Authority must exercise his control and assessment powers in compliance with such principles. The fundamental expression of the involvement of the taxpayer in the public administration decision is the “right to be heard”, intended as anticipation of the future activities of the administration. Precisely, it is a phase of research, acquisition and assessment of the evidence and of any other information which may facilitate a better reconstruction of the application of the tax (“presupposto”). In these terms, the “right to be heard” is an implementing tool for taxpayer’s right of defense and for best practice in the public administration. Therefore, it should be mandatory, always and in any case, in accordance with art. 3 and art. 97 of Italian Constitution, and with European law. However, this assumption is not found to be peaceful.

Keywords: tax law, right to be heard, involvement of the taxpayer, tax authority decision

1. Introduction

The relationship between taxpayers and Tax Authority and the involvement of the taxpayer in the public administration decision is a very important area of investigation in Italian tax law [1].

This relationship is based on equity and cooperation in good faith, which stems from constitutional principles, such as the principle of sound administration (Art. 97 Italian Constitution), fairness and solidarity (Art. 3 Italian Constitution).

Therefore, Tax Authority must exercise his control and assessment powers in compliance with such principles.

The fundamental expression of the involvement of the taxpayer in the public administration decision is the “right to be heard”, intended as anticipation of the future activities of the administration. Precisely, it is a phase of research, acquisition and assessment of the evidence and of any other information which may facilitate a better reconstruction of the application of the tax (“presupposto”). In these terms, the “right to be heard” is an implementing tool for taxpayer’s right of defense and for best practice in the public administration. Therefore, it should be mandatory, always and in any case, in accordance with art. 3 and art. 97 of Italian Constitution, and with European law.

However, as will be seen, this assumption is not found to be peaceful in national and European laws and in the interpretation of domestic and supranational jurisprudence. Therefore, it is necessary to reflect on the appropriate instruments to make it a fundamental principle at the base of the relationship between taxpayer and tax administration.

2. The involvement of the taxpayer in the tax authority decision in Italian tax law

The duty to file the tax return is central and represents the most important expression of cooperation with the Tax Authority, since it allows to know the condition for the application of the tax (“presupposto”) and the relevant sources of income, and also to calculate the taxable income.

Furthermore, art. 32 D.P.R. of 29 September 1973, No. 600, identifies Tax Authorities’ investigative and assessment powers: therefore, taxpayers’ duties may be identified “in negative”.

Firstly, Tax Authority may invite taxpayers to provide data and information, as well as to produce documents useful to assess the taxable income and issue a tax assessment notice.

Tax Authority may also require to the taxpayers subject to accounting duties, to provide the profit and loss account and other accounting records. Moreover, Tax Authority may send specific questionnaires aimed at collecting detailed data and information relevant to the tax assessment, and they have full access to all bank information regarding taxpayer’s transactions. Such questionnaires should be filled in, signed by the taxpayers and returned to the Tax Authority. In addition, art. 32 D.P.R. of 29 September 1973, No. 600, lays down a general prohibition for the taxpayer to produce during tax litigation all the documents required (but not exhibited) during the tax assessment phase.

Tax Authority has also the right to request information to third parties, who are, therefore, subject to a general duty of co-operation.

Another example of the duty of cooperation between taxpayers and Tax Authority is the “audi et alteram partem” mechanism [2], provided by art. 38 D.P.R. of 29 September 1973, No. 600, in line with the right to defense, in the synthetic assessment (so-called “expenditure assessment system”) [3], and by art. 10-bis Law of 27 July 2000, No. 212 (entitled rights and safeguards of taxpayers subject to tax audits), that regulates tax avoidance and abuse of law [4].

As well as, with respect to tax audits, Art. 12, para. 2, Law of 27 July 2000, No. 212 provides that taxpayers have always the right to be informed about the reasons justifying the tax audit, the object and the transactions analyzed, as well as the right to be assisted by a professional advisor – who shall represent and assist the taxpayer in tax litigation against ITAs – and all other rights and duties enjoyed by the audited taxpayer. Moreover, according to art. 12, para. 7, Law of 27 July 2000, No. 212, the audited taxpayer has the right to provide written comments within 60 days after the delivery of the tax audit report [5].

The tax system provides also some “indirect” or “improper” sanctions, which, in presence of behaviors not corresponding to the requirements of collaboration and good faith, prevent or reduce the taxpayer’s right to defense both in the administrative phase and in the one before the Tax Court [6].

Furthermore, in the Italian tax system there are various kinds of advance ruling, with different procedures, but all of them have in common the specific aim to give taxpayers the possibility to request (and obtain) a decision from the Tax Authority concerning the correct application and interpretation of certain tax rules applicable to a concrete situation.

Advance ruling procedures are, essentially, instruments aiming to give the taxpayer the right to know in advance Tax Authority approach in case of objective uncertainty: consequently, those instruments allow the taxpayer to behave in line with such approach.

The protection of the taxpayer’s legitimate expectations at the end of the advance ruling procedure is the basic reason that motivates the effects on these mechanisms on administrative tax penalties [7].

In the direction of the cooperation between taxpayers and Tax Authority moves also the agreement on the notice of assessment (so called “accertamento con adesione”), that allows the taxpayer to reduce its tax liability, avoiding to engage a tax litigation before the Court: this procedure, which may be started by the Tax Office or by the taxpayer, allows the parties to reach an agreement that re-determine the taxpayer’s tax liability [8].

However, the measures described above do not seem to be sufficient in order to ensure the involvement of the taxpayer in the tax authority decision, mostly because such involvement is not fully available for taxpayers in every procedure.

In fact, for the taxpayer’s full participation in the tax authority decision, to the taxpayer should always be acknowledged the “right to be heard”, on which we will discuss in detail below.

3. The “right to be heard” in tax proceedings in Italian Supreme Court case law

The Italian Supreme Court (ISC) has enhanced the “right to be heard”, since the decision 29 July 2013, n. 18184, Joint Sections [9].

With the decision n. 19667 and n. 19668 of 18 September 2014, the ISC reiterated the existence of the “right to be heard” even if tax laws have not at provided this right, as occurred in the case of the registration of a mortgage according to art. 77 D.P.R. n. 602 of 1973 to guarantee tax credits.

A further step forward in the definition of the problem came from the ordinance of ISC n. 527 of 14 January 2015, concerning the checks carried out at the office of the tax authority.

However, precisely with regard to the checks carried out at office of the tax authority, the subsequent sentence of ISC, Joint Sections, 9 December 2015, n. 24823, has changed its orientation.

The ISC, which reaches conclusions diametrically opposed to the previous decision n. 19667/2014, after a long excursus of the previous jurisprudence of the same Court, affirms that the guarantees provided by the art. 12, paragraph 7, of the law n. 212/2000 operate only in the presence of tax audits carried out where the taxpayer takes its activity and not in other cases. This is because there is a number of legislative provisions that prescribe the “right to be heard” in different times, but there is not an express legislative provision that provide in general the obligation of the “right to be heard” in every tax procedure.

The Court’s thesis is not to be shared. This is because the widespread presence of norms that provide the “right to be heard” leads us to believe, where we proceed with an interpretation oriented by the art. 3 and 97 of the Constitution, that exists a general principle and that the plurality of provisions is linked to the need to provide different methods of contradictory procedure in relation to the specific tax assessment method adopted [10].

Furthermore, cannot be shared the Supreme Court’s argument that the “right to be heard,” which derives from the European legal system, is applicable only in the case of an investigation concerning the taxes harmonized.

In fact, the tax assessment notice, which concludes the proceeding, is normally based on facts that regard at the same time a tax claim both as VAT (harmonized tax) and as IRPEF (or IRES) and IRAP (taxes not harmonized). In the case of non-compliance with the principle of the “right to be heard”, in presence of the same facts, would be issued in the same tax assessment procedure a partial, rather than total, judgment of the act.

Furthermore, cannot be shared the Supreme Court’s argument that the “right to be heard,” if not provided by law, is allowed only if, in accordance with the jurisprudence of the Court of Justice, it is shown that, in the absence of such irregularities, the tax procedure could be concluded with a different result [11].

This last statement raises a lot of perplexity, considering that the outcome of a dispute, according to the principle of legal certainty, cannot be entrusted to an assessment, inevitably

uncertain, about the outcome that the judgment would have had in the presence of a contradictory procedure which in reality did not take place.

4. The “right to be heard” in tax proceedings as a general principle of European law

The supremacy of European law (EU), through the European Court of Justice (ECJ), has influenced the exercise of national tax sovereignty within the European Union [12].

The supremacy of EU law is the key to understanding how taxation has evolved within the European Union from a purely national to a supranational dimension [13].

The impact of ECJ case law on Italian taxation reveals a fairly extreme picture of the critical issues that arise in such a context.

The impact of ECJ case law on administrative tax practice within the framework of tax auditing and collection procedures involves aspects that can also be relevant from the perspective of ensuring the protection of human rights [14].

From the perspective of ECJ case law, the principles of proportionality and suitability may be invoked to prevent unreasonable inspections, or the payment of guarantees that would not be needed to protect the interest of the tax authorities (based on the line of reasoning developed by the ECJ in *de Lasteyrie* (C-9/02) 11 March 2004).

Likewise, the ECJ regards the *audiatatur et altera pars* principle as a general principle of EU law, which gives taxpayers the “right to be heard” before a tax measure affects their personal sphere (Case C-349/07, *Sopropé* (18 December 2008, Para. 36).

Similarly, following ECJ case law, the duty of cooperation on the part of tax authorities should require them to reopen a final administrative tax act based on misinterpretation of (or a conflict with) EU law when this is allowed under national procedural law and the person directly affected has, in a timely manner, filed a complaint against such an act (Case C-453/00, *Kühne & Heitz* (13 January 2004, Para. 28).

In this direction we can also consider the case law of ECJ 12 February 2015 (C-662/13) and the case law 3 July 2014 (C-129/13 and C-130/13) *Kamino International Logistics BV and Datema Hellmann Worldwide Logistics BV*.

However, the jurisprudence cited above added a provision which could give rise to ambiguity, stating that the national court, having the obligation to ensure the full effectiveness of Union law, in assessing the consequences of an infringement of the right of the defense, in particular “the right to be heard”, can consider that such infringement leads to the annulment of the final decision taken at the end of the administrative procedure only if, in the absence of such irregularity, that procedure could have led to a different result.

In this way the Court has opened to an interpretation that diminishes the same value of contradictory procedure, evaluating it on the proof that the result of the administrative procedure would have been different.

However, even the European treaties provide the “right to be heard” [15].

In particular, art. 6 of the Treaty on the Functioning of the European Union undoubtedly guarantees substantial rights of the person. And so also art. 6 of the European Convention on Human Rights, which until now has found peaceful application in the protection of domicile and correspondence and in the application of sanctions, although not yet in the matter of taxes.

In the same way art. 41 of the European Charter of Fundamental Rights, which has the same legal value as the European treaties, establishes the right to good administration.

5. The “right to be heard” in tax exchange of information proceedings

Exchange of information is a fundamental tool for cooperation between national financial administrations. In recent years, we have witnessed a significant evolution of the discipline of the phenomenon in the European and international level, which has led to an increasingly evident need for mutual support between administrations in order to fight tax avoidance. International organizations have set many goals aimed to fighting cross-border tax avoidance, including the implementation of internationally recognized cooperation, understood as an obligation of collaboration between the administrations.

In European legislation, the main source of exchange of information is contained in Directive 2014/107/EU (which has put an end to bank secrecy for tax purposes throughout the Union, is also of particular relevance, requiring Member States to automatically exchange a wide range of information on incomes and holdings abroad), than modified by Directive 2015/2376 and Directive 2016/881/EU on the mandatory automatic exchange of information in the tax field. Among the sources of international law, the main rule is art. 26 of the OECD Model Convention against Double Taxation. The need for states to get information more rapidly and automatically has led the European and international institutions to the elaboration of additional tools for data exchange. However, in the face of a strong development of regulatory instruments for implementation of the exchange of information, particular attention should be paid to the profile of the protection of the rights of the taxpayer, currently debated in the European case-law and without specific discipline in the international and community sources. It is clear that the taxpayer has a particular interest in the correct acquisition of news and data and the confidentiality of the information exchanged [16].

The absence of a specific discipline in the international and European sources which guarantees the protection of the taxpayer when exchanging information can lead to a number of issues: just thinking to the case of a state which violates the limits set for the exchange of information by disclosing a secret commercial or professional.

In fact, it is not foreseen that the taxpayer will be informed of the request for information made on his behalf by the financial administration of another state. Consequently, its right to

oppose to that transfer of information it is not recognized and even the opportunity to expose its reasons in the course of investigation.

The protection of the taxpayer in the exchange of information is therefore subject to rules of national law on the exercise of the instructing powers by the financial administration.

The subject may therefore oppose the procedure by maintaining that it is illegitimate only if one of the countries involved in the exchange established precise provisions on this. In some jurisdictions, like in the Italian one, the protection of the rights of the taxpayer appears subordinate to the appeal of the subject against an act emanated to him. In case the inquiry concerns information requested by another administration, the lack of administrative or judicial tools available for the taxpayer seems to make it impossible for any action to protect the injury of his rights.

On 22 October 2013, the Court of Justice of the European Union (ECJ) issued an important judgment in the case of *Sabou v. The Czech Republic* (Case C-276/12) concerning the application of the right of defense in the context of tax information exchange procedures. This was the first decision where the ECJ addresses the protection of the taxpayer's right of defense in the framework of international mutual assistance procedures in tax matters. In this regard, the ECJ adopted a twofold approach, considering both the provisions of the former Directive (the previous one n. 77/799/EEC) and the fundamental "right to be heard".

So, the problem is the fact that tax authorities are not bound to confer on taxpayers the "right to be heard" during the information-gathering stage, which includes both actions undertaken in the requesting state and those carried out by the requested Member State.

Therefore, it could be said that the right of defense, considered a general principle of EU law and also laid down in art. 41 of the Charter of Fundamental Rights of the European Union (EU Charter), does not oblige the requested state to inform the taxpayer about the existence of a request for information concerning him, the data-gathering process or the transmission of the information to the requesting state.

Notwithstanding this, the ECJ established a kind of twofold "balancing mechanism" from the point of view of the taxpayer's rights of defense: firstly, the "right to be heard" (as a general principle of EU law) should be granted before any decision is adopted at the end of the administrative proceedings by the tax authorities of the requesting Member State and, secondly, the affected taxpayer should be able to challenge, in accordance with its domestic rules and procedures, the accuracy and probative value of the information provided by the requested state in the context of tax proceedings within the requesting Member State where such information is used.

The *Sabou* decision shows that the fundamental right of defense of taxpayers affected by an exchange-of-information procedure in the requesting state (usually the country of the taxpayer's residence) is linked to the administrative and/or judicial proceedings implemented by the tax authorities of the requested state in order to gather the information. However, and despite such "interconnection", it must be clear that the rights of the taxpayer affected by the request for information in the requested state are independent of those which can be conceded by the requesting state.

A step forward compared to the Sabou decision was obtained with the decision 16 May 2017, Berlioz (C-682/15), in which ECJ established that the taxpayer can legitimately access, at least in part, the file of the exchange information, without any opposition to the protection of diplomatic relations between States.

6. Conclusion

In order to ensure an efficacious involvement of the taxpayer in the tax authority decision as alternative to the tax litigation, so as to bring the relationship between taxpayers and Tax Authority on equity and cooperation in good faith, it is necessary that the “right to be heard” become a mechanism fully available for taxpayers in every procedure.

Also because such principles, it should be noted, stem from constitutional principles, such as the principle of sound administration (Art. 97 Italian Constitution), fairness and solidarity (Arts. 3 Italian Constitution).

In general terms, it can be said that contradictory procedure or the participation of private individuals in the formation of acts of the public administration is a juridically protected instrument; has acquired, that is, the dignity of a guaranteed legal “good” in favor of the citizen [11].

So, the “right to be heard” is a fundamental right of all participants in an administrative procedure, and they can make use of this right throughout the entire procedure, making allegations and submitting documents; this right is formalized in the hearing that must take place immediately before the administration makes a decision [17].

The “right to be heard” must always be possible, so as not to create unequal treatment between harmonized and non-harmonized taxes and allow the respect to the constitutional principles.

As well as, in tax exchange of information proceedings, it should be implemented specific “participation rights” to safeguard the legitimate interests of taxpayers affected by cross-border requests of information in different administrative or judicial proceedings. Those “participation rights” should include the notification of the request for information to the taxpayer; the “right to be heard” before transmitting the information to the requesting state, and the right to challenge the decision of the requested state concerning the transmission of the information gathered.

It is therefore necessary to state that the recipient of a tax claim, whether harmonized or not, interests or penalties, has the right to be informed before the proceedings are completed by issuing the act in which the tax claim is expressed. The right of the recipient to be informed before being harmed is undeniable [11].

There is a general principle according to which the recipient of a tax claim has the right to contradictory procedure, that is to express his point of view in contrast with that of the Financial Administration before the final act is issued.

It can be concluded by stating that the recognition of obligations for the public financial administration, corresponding to as many rights for the recipient of the tax claim, and assisted, in the event of non-compliance, from the penalty of the abolition of its provisions, far from favoring tax evasion, is a stimulus to the observance of fiscal obligations in a state of legality and collaboration.

Disclaimer

Michele Mauro is Author of paragraphs n. 5 and n. 6. Claudia Fava is Author of paragraphs n. 1 and n. 2. Alessandra Kostner is Author of paragraphs n. 3 and n. 4.

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