

*Editors:* Chris Evans, Judith Freedman, Richard Krever



# The Delicate Balance

Tax, Discretion  
and the Rule of Law

**IBFD**

# The Delicate Balance: Tax, Discretion and the Rule of Law

## Why this book?

Few aspects of revenue law generate stronger feelings than the exercise of discretionary power by tax administrations. A delicate balance often needs to be struck between the legitimate needs of revenue authorities and the equally legitimate interests and rights of taxpayers. On the one hand, the executive and administration need to have sufficient capacity to apply the law; on the other, there is a need to maintain the principle of the rule of law that it is the elected legislature, and not the executive or tax administration, that establishes tax burdens. The chapters in this volume explore that delicate balance.

The Delicate Balance - Tax, Discretion and the Rule of Law considers the critical questions that arise from the intersections of tax, discretion and the rule of law in modern common and civil law jurisdictions: What do we mean by tax discretion and how does it vary in conceptual and practical terms in different tax regimes? What role should discretion play in tax systems that operate under the rule of law and how large should that role be? What are the legal, political, institutional and other constraints that can prevent abuse of discretion? To what extent can, and should, the legislature safely delegate discretionary powers to tax administrations?

This book is the outcome of a conference held in Prato, Italy in September 2010 and sponsored by the Oxford University Centre for Business Taxation together with the Department of Business Law and Taxation at Monash University and the Australian School of Taxation and Business Law (University of New South Wales).

<b>Title:</b>	The Delicate Balance
<b>Subtitle:</b>	Tax, Discretion and the Rule of Law
<b>Editor(s):</b>	Chris Evans, Judith Freedman et al
<b>Date of publication:</b>	September 2011
<b>ISBN:</b>	978-90-8722-103-4
<b>Type of publication:</b>	Print Book
<b>Number of pages:</b>	368
<b>Terms:</b>	Shipping fees apply. Shipping information is available on our website
<b>Price:</b>	EUR 110 / USD 150 (VAT excl.)

## Order information

To order the book, please visit [www.ibfd.org/IBFD-Products/shop](http://www.ibfd.org/IBFD-Products/shop). You can purchase a copy of the book by means of your credit card, or on the basis of an invoice. Our books encompass a wide variety of topics, and are available in one or more of the following formats:

- IBFD Print books
- IBFD eBooks – downloadable on a variety of electronic devices
- IBFD Online books – accessible online through the IBFD Tax Research Platform



IBFD, Your Portal to Cross-Border Tax Expertise

---

## Table of contents

<b>Preface</b>	v
<b>Tax, Discretion and the Rule of Law</b>	1
<i>Dominic De Cogan</i>	
1. Background	1
2. Defining “discretion”	2
3. Discretion and legal systems	4
3.1. The source of discretion	4
3.2. The exercise of discretion	5
3.3. Tax discretions compared	7
3.3.1. Judicial review	7
3.3.2. Binding the tax authority	8
3.3.3. Binding the taxpayer	9
3.3.4. Trust	10
3.3.5. Institutions	11
4. Critique and reform	12
4.1. The source of discretion	12
4.2. The exercise of discretion	13
4.3. Reform	13
5. Conclusion	14
<b>The Delicate Balance: Revenue Authority Discretions and the Rule of Law – Some Thoughts in a Legal Theory and Comparative Perspective</b>	15
<i>Ana Paula Dourado</i>	
1. Introductory remarks: is discretion exercised by the revenue authorities?	15
2. The rule of law	16
2.1. The legal type of tax	16
2.2. Validity and legitimacy	16
2.3. The rule of law and parliamentary laws	18
3. Legal determinacy and creation vs. application	20
4. The framework for delegations to the government and to the revenue authorities	24

## Table of Contents

---

5.	Delegation to the government	25
6.	Vagueness and indeterminacy in tax law	27
7.	Legal techniques and the rule of law: tax law between “typifying” and vagueness	29
8.	The meaning of revenue authority discretions	30
9.	Common law vs. civil law countries	31
10.	Administrative and judicial typifying	33
11.	Conclusions	34

### **The Promise and the Reality of U.S. Tax Administration** 39 *Kristin E. Hickman*

1.	The U.S. delegation compromise	42
2.	Tax administration deviations	50
2.1.	Temporary Treasury regulations	50
2.2.	Guidance documents	53
2.3.	Limited judicial review	55
3.	The implications of imbalance	57
4.	Conclusion	62

### **A Reasonable Balance: Revenue Authority Discretions and the Rule of Law in Canada** 63 *Kim Brooks*

1.	Canada’s porous separation of powers	63
2.	The three branches in theory	64
2.1.	The legislative branch	64
2.2.	The executive branch	65
2.3.	The judicial branch	68
3.	The good sense of blurring the three functions in practice	69
4.	A reasonable balance in action: the taxation of in-kind benefits	74
5.	An appropriate allocation of discretion	77

<b>HMRC's Management of the U.K. Tax System:</b>		
<b>The Boundaries of Legitimate Discretion</b>		79
<i>Judith Freedman and John Vella</i>		
1.	The revenue authority's discretion and its limits	79
1.1.	Constitutional principles	80
1.2.	Discretionary powers of the U.K. revenue authority	80
1.3.	Secondary legislation	81
1.4.	Control of discretion	83
1.4.1.	Courts	83
1.4.2.	Parliament	83
1.4.3.	Internal procedure and other bodies	86
1.5.	Chapter outline	87
2.	Constitutional limits on HMRC discretion	87
2.1.	The framework dictated by the supremacy of Parliament principle	87
2.2.	The principle of legality	89
2.3.	Remaining constitutional principles	90
2.3.1.	Article 4 of the Bill of Rights Act 1689	91
2.3.2.	The rule of law	93
2.3.3.	Human Rights Act 1998	98
2.3.4.	EU law	100
3.	Judicial review and HMRC discretion	100
3.1.	Legitimate expectations	102
3.1.1.	The limits of the legitimate expectation principle	103
3.1.2.	The limits of guidance	104
3.1.3.	The value of the legitimate expectations doctrine in controlling revenue discretion	108
4.	HMRC's general discretion: categories and issues	108
4.1.	Category A: discretion as to non-application of the law where its proper interpretation is agreed	109
4.1.1.	Extra-statutory concessions	109
4.1.2.	Waivers and deals	111

## Table of Contents

---

4.2.	Category B: discretion as to how to interpret the law	112
4.2.1.	Statements of Practice, guidance and manuals	112
4.2.2.	Clearances	114
4.3.	Category C: discretion in management of legislation and litigation	115
4.4.	Category D: hybrids of the above categories	116
5.	Conclusion	118

### **The Delicate Balance: Revenue Authority Discretions and the Rule of Law in Australia** 121

*Michael Walpole and Chris Evans*

1.	Introduction	121
2.	An expression of the rule of law	123
3.	The Commissioner's powers	127
3.1.	Formal administrative powers	127
3.2.	Powers of interpretation	128
3.3.	Discretionary powers	129
3.3.1.	Liability discretions	130
3.3.2.	Administrative discretions	131
3.3.3.	Anti-avoidance discretions	132
4.	The Commissioner and the courts	133
5.	Principle-based drafting	138
6.	Extra-statutory concessions	142
6.1.	Background	142
6.2.	The Tax Design Review Panel	142
6.3.	The Treasury Discussion Paper	143
6.4.	Responses to the Treasury Discussion Paper	145
7.	Conclusions	147

### **Revenue Authority Discretions and the Rule of Law in New Zealand** 149

*Shelley Griffiths*

1.	Introduction	149
2.	Discretions and the rule of law – the New Zealand context	150

3.	Discretion in the Income Tax Act	152
4.	Discretion in tax administration	155
4.1.	The managerial discretion of the New Zealand Commissioner of Inland Revenue, sections 6 and 6A of the Tax Administration Act 1994	156
4.2.	Settlement	162
4.3.	Reassessment	168
5.	Conclusion	170
6	Responsibility on Ministers and officials to protect integrity of tax system	172
6A	Commissioner of Inland Revenue	172

**Revenue Authority Discretions and the  
Rule of Law: South Africa** 175  
*Ernest Mazansky*

1.	Introduction	175
2.	Constitutional background	175
3.	Levying of tax	177
4.	The South African Revenue Service	178
5.	Concept of the rule of law	179
6.	Discretionary powers	181
7.	Safeguards for taxpayers	184
8.	Objection and appeal procedures in the tax laws	185
9.	Discretions	186
10.	Delegated rule-making powers	187
11.	Interpretation notes and guides	188
12.	Binding rulings	190
13.	Extra-statutory concessions	190
14.	Trends towards strengthening the rule of law in taxation matters	190
15.	Some general observations	191
16.	Some practical aspects	192
16.1.	Write-off of tax debts	192
16.2.	Settling a dispute	194
16.3.	Tax controversy	195
16.4.	Advance rulings	196
17.	Concluding remarks	199

**Revenue Authority Discretions and the Rule of Law  
in Hong Kong** 201

*Andrew Halkyard*

1. Background and history of income tax in Hong Kong 203
2. The constitutional position in relation to the imposition  
of taxation in Hong Kong 204
3. Taxation legislation in Hong Kong and the role of  
discretion 205
4. Administration of tax law in Hong Kong – co-operation or  
confrontation? 210
5. Commitment to service and the Taxpayers’ Charter 211
6. Extra-statutory concessions—their status and authority 213
7. The pervasiveness and importance of  
departmental practice 215
8. Conclusions 216

**Balancing of Powers in Dutch Tax Law: General  
Overview and Recent Developments** 223

*Richard Happé and Melvin Pauwels*

1. Introduction 223
2. Some important characteristics of Dutch  
constitutional practice 224
  - 2.1. Limited power of judiciary to test Acts of  
Parliament 224
  - 2.2. The central role and “two hats” of the State  
Secretary of Finance 225
  - 2.3. Traditional discretionary power of the tax  
administration 228
3. Balancing of legislative and judicial power 228
  - 3.1. Introduction 228
  - 3.2. The judiciary’s testing of Acts of Parliament for  
compatibility with the principle of equality 229
  - 3.3. Overruling of case law by the legislature 231
4. Balancing of executive and judicial power 233
  - 4.1. Introduction 233
  - 4.2. More procedural room for the tax administration 234
  - 4.3. The phenomenon of “enforcement covenants” 234
5. Balancing of legislative and executive power 237
  - 5.1. Introduction 237



5.2.	Shift of power from legislature to executive	237
5.2.1.	Simplicity of legislation	238
5.2.2.	Rule-making by the executive	239
5.2.3.	Discretionary power	240
5.3.	Countervailing balance by the judiciary?	241
6.	The judiciary's response to the discretionary power of the tax administration when applying tax legislation	245
6.1.	Introduction	245
6.2.	Potential issues	246
6.3.	Applying principles of proper government behaviour by the judiciary: priority rules	247
6.4.	Conclusion	248
7.	Conclusion	249
7.1.	General framework	249
7.2.	Legislative power vs. judicial power	250
7.3.	Executive power vs. judicial power	251
7.4.	Legislative power vs. executive power	252

**The Delicate Balance Between Revenue Authority Discretions and the Rule of Law in France** 255  
*Christophe Grandcolas*

1.	Introduction	255
2.	Current situation	260
2.1.	Main types of advance binding rulings issued by the tax authorities	261
2.2.	Procedures to request and issue advance rulings	266
2.2.1.	Procedure to submit applications	266
2.2.1.1.	How to present an application?	266
2.2.1.2.	To whom should an advance ruling application be submitted?	267
2.2.1.3.	When?	268
2.2.1.4.	Free?	268
2.2.1.5.	Scope?	268
2.2.2.	Responses	269
2.2.2.1.	In writing or tacit?	269
2.2.2.2.	Delays	269
2.2.2.3.	Can the ruling be disputed?	270

# Tax, Discretion and the Rule of Law

Dominic De Cogan\*

## 1. Background

Few aspects of revenue law generate stronger feelings than the exercise of discretionary power by tax authorities. The eminent English judge Lord Hewart, writing in 1929, used income tax discretions as an “extreme” illustration of the dangers posed by the ascendancy of government over Parliament and courts:<sup>1</sup>

Let it be supposed [...] that the power of deciding disputes as to liability to income-tax were vested in the Board of Inland Revenue, without appeal to the Courts. “Oh,” it may be said, “but that is an extreme case which would never be sanctioned by Parliament.”

The Carter Commission reported some rather more sympathetic views, including the following observations of the Canadian Minister of Finance in 1948:<sup>2</sup>

There are some situations where ministerial discretion is the only fair way to have certain questions settled. It is a device which avoids the rigidity of a written statute, and it is a means whereby real cases of hardship may be avoided. Frequently the law cannot anticipate all the situations which may arise, and in the absence of ministerial discretion there is no alternative to enforcing the letter of the law.

Such widely differing attitudes on the proper quantity and quality of discretion in taxation can be difficult to relate to each other, in large part because there is no generally agreed discourse under which basic questions may be addressed clearly. What is tax discretion? Should it be eradicated or accommodated? How might it be improved? The matter is complicated further by the highly contextual and dynamic nature of tax regulations, as these striking comments of the U.K. Inland Revenue in 1944 illustrate:<sup>3</sup>

---

\* Ph.D. Candidate in Tax Law, University of Cambridge.

1. Lord Hewart C.J., *The New Despotism* (London: Ernest Benn Ltd., 1929), p. 46. The chapter heading is “Administrative Lawlessness”.

2. Royal Commission on Taxation (Carter Commission), “Legislation, Administration and Interpretation Process in Federal Taxation”, Study No. 22 (Montreal: Queen’s Printer, 1964), p. 93.

3. Board of Inland Revenue, Notes on Finance Bill 1944, Committee Stage, p. 54.

Even in peace-time it is not unknown to have a definitely extra-statutory taxation arrangement which involves a definite departure from the strict rule of the law, though it has always been the policy of the [government] to challenge any such extra-statutory arrangement and report it as a matter which should be covered by statutory provision in a Finance Act. But the circumstances of war-time are very different, and there have been a large number of extra-statutory concessions relating to Inland Revenue duties.

The powers of tax authorities to determine aspects of liability, and trends in these powers, must therefore be justified in the light of all relevant circumstances. This is not always achieved satisfactorily, and particular vigilance is needed that discretionary powers are not shifted progressively to revenue officials, without sufficient reason and to the detriment of traditional rule of law values. It is important that a common language is developed, with which these matters may be discussed and contested openly.

The present volume represents a sustained attempt to address this problem, as a matter of theory but also with close reference to ongoing controversies in twelve different common and civil law jurisdictions. In line with the comments above, the contributions focus on the relations between tax discretion and the rule of law, within the wider context of constitutional allocations of power and the more general relations of citizen and state. There are certain variations in emphasis and perspective between chapters that result from the differences in fundamental assumptions in the jurisdictions represented. Nevertheless, the common themes are strong, and the following three questions are discussed in almost every chapter of the volume:

1. What is tax discretion?
2. What is the place of discretion within tax systems?
3. How should tax discretion be reformed?

The remaining sections below review each of these items in turn, outlining some of the main issues discussed elsewhere in the volume and starting with the meaning of “discretion”.

## **2. Defining “discretion”**

An explanation of tax discretion might be approached from two directions. First, a *descriptive* definition might be offered, that explained the source or consequences of the powers in question. Secondly, a *normative* account

might be favoured, that described an ideal system of tax rules and showed the role that discretion would play within its proper context. Underneath these headings, further distinctions might be made. Discretions explicitly delegated by statute may be compared with those inherent in the interpretation of legislation, or powers exercised by officials but which lack a clear basis in law. A descriptive approach looking to consequences could divide between *liability* discretions that, potentially, affect the amounts of tax payable; *administrative* discretions that encompass such matters as tax forms, investigations and time limits; *anti-avoidance* regimes; *temporary* rule-making powers in anticipation of detailed statutory regulation; and so forth.<sup>4</sup>

The views of commentators on the precise content of discretion inevitably differ, but it is critical that these are articulated adequately. This is natural for normative accounts of tax discretion, where the underlying theoretical concerns of the author will be reflected throughout their exposition of the desired structure of tax rules and the place of discretion therein.<sup>5</sup> Yet even descriptive approaches require to be explained to the reader. For example, many analysts, drawing upon their understanding of constitutional requirements, would refuse to classify extra-statutory concessions as discretions at all, preferring to regard them as plainly illegal.

This highlights a further point, that apparently objective descriptions of “discretion” appear to be influenced by the underlying structure of tax rules. Wide delegations of power to the authorities, in particular, would seem to blur the conceptual lines between the exercise of delegated authority and other activities such as interpretation or extra-statutory concession. The *Fleet Street Casuals* decision in the U.K., for instance, confirmed that the power of “care and management” enjoyed by the Inland Revenue authorized the selective enforcement of existing tax liabilities.<sup>6</sup> That the problem reached the House of Lords, the highest domestic court, illustrates the difficulty of distinguishing strictly between lawful delegation and unlawful concession. The position of the United States is also noteworthy in this regard, the Treasury exercising a general power to promulgate tax

---

4. See Walpole, Michael and Chris Evans, “The Delicate Balance: Revenue Authority Discretions and the Rule of Law in Australia” (this volume).

5. See Dourado, Ana Paula, “The Delicate Balance: Revenue Authority Discretions and the Rule of Law – Some Thoughts in a Legal Theory and Comparative Perspective” (this volume).

6. *Inland Revenue Commissioners v. National Federation of Self-Employed and Small Businesses Ltd.* [1982] A.C. 617 (*Fleet Street Casuals* case). See Freedman, Judith and John Vella, “HMRC’s Management of the U.K. Tax System: The Boundaries of Legitimate Discretion” (this volume), text at nn. 132 and 135.

regulations despite a nondelegation doctrine in the U.S. Constitution that is arguably applicable.<sup>7</sup>

In other jurisdictions, by contrast, the transfer of power from the legislature to the tax authorities is much more strictly circumscribed, whether by an ingrained culture of seeking a clear statutory justification for administrative action, the intervention of courts or for other reasons. In these instances there seems to be a much sharper conceptual separation between “discretion”, which is equated with authority specifically delegated by the legislature, and the varied other functions of the tax administration. The implication of this is that descriptive definitions of discretion are not immune from normative considerations, on what administrators should be permitted to do within the constitutional context and how this should be authorized. Even this first stage of defining the word discretion, then, is laden with values.

### **3. Discretion and legal systems**

The detailed discussion in later chapters on the position of tax authority discretions within legal systems is dominated by three closely associated ideas, namely the separation of powers; consent to taxation through the democratic process; and the rule of law. The emphasis to be placed on each of these concepts varies depending on the outlook of each author, and on the constitutional discourse that prevails in different jurisdictions. A recurring theme throughout this volume, however, is a basic insistence that tax discretions should be treated as an integral part of the legal system and judged to the same – if not higher – standards of legitimacy as other forms of administrative law. These matters are discussed conveniently under two broad headings, as follows: first, is the discretion legitimate in its source; secondly, is the discretion legitimate in its exercise in practice?

#### **3.1. The source of discretion**

In many jurisdictions the source of discretionary power is associated closely with the doctrine of separation of powers. The starting point, at least under a pure version of the doctrine, might be that rule-making should

---

7. See discussion in Hickman, Kristin, “The Promise and the Reality of U.S. Tax Administration” (this volume), text at nn. 12-17.

be reserved entirely to legislators. It is widely appreciated, nevertheless, that the demands of modern administration justify a level of delegation to the tax executive. The spirit of the separation of powers doctrine, it is felt, may be upheld provided that the courts enjoy both legal and practical wherewithal to police the activities of tax authorities.<sup>8</sup> In other words, the decrease in the influence of legislators would be compensated for by the enhancement of judicial power. This line of reasoning is not adopted universally and in some jurisdictions there is a strong tradition of direct appeal to the need for democratic consent to taxation. The natural forum for tax debate, on this view, is the legislative body, even if it is accepted that legislators enjoy formal powers of delegation. Tax authority discretions represent a departure from this general principle and need therefore to be explained and justified.

It is interesting to speculate on whether such direct appeals to democracy entail a greater intolerance of delegated discretion than a separation of powers analysis. A deficit of democratic debate would, on its face, be less susceptible than a breach of the separation of powers doctrine to “cure” through the oversight of the courts. There is a possibility, though, that discretionary decisions of the tax authorities might be enhanced with procedures for taxpayer or citizen participation that could replicate many of the democratic advantages of conventional legislation.<sup>9</sup> In other words, the risk of unfairness would be alleviated by imposing democratic discipline upon subordinate decision-makers. The opposite process is also possible, unfortunately, whereby robust regulatory procedures are sidestepped by the routine use of informal rules, which may or may not have binding legal effect. Care must be taken, moreover, that improved structures for the performance of discretionary responsibilities are not used as a mere pretext for the more general shift of power from the legislature to the tax authorities.

### 3.2. The exercise of discretion

Assuming that discretionary or regulatory power has been delegated validly, it may, nonetheless, be used in better or worse ways. In the course of preparing their chapters in this volume, authors have found it useful to

---

8. See section 3.3.1, *infra*.

9. See Hickman (this volume), text at nn. 29-38.

refer to the seminal legal and constitutional theories of Fuller,<sup>10</sup> Dicey,<sup>11</sup> Raz<sup>12</sup> and Krygier,<sup>13</sup> and to the official advice of the United Nations,<sup>14</sup> in order to articulate concrete standards for the exercise of discretion. A more detailed exposition of these matters can be located in the chapters by Dourado, Freedman and Vella, Walpole and Evans, Griffiths and Mazansky, but some common themes are as follows. The law of taxation, including its discretionary elements, should be clear; capable of guiding taxpayers; stable; fairly enforced; non-retrospective; capable of implementation; and open to adjudication before an independent tribunal.

These requirements, which are typically discussed in connection with the “rule of law”, could impose deep limitations on the exercise of delegated power. This may hold its attractions, but it seems equally certain that rule of law values do not express every characteristic that is desirable in a tax system.<sup>15</sup> On the contrary, they may need to be balanced against other considerations such as the efficient administration of the tax system, the distribution of burdens in accordance with ability to pay or otherwise. It would also be mistaken to equate the rule of law with exhaustive primary legislation, and indeed there is an argument that an excess of statutory detail is counterproductive, makes the law overly complicated and is difficult for taxpayers to follow. Furthermore, detail does not necessarily resolve problems of interpretation and application, which may resurface in the guise of inflexibility or in uncertainties around the treatment of gaps in the law.<sup>16</sup> Less detailed primary legislation does not necessarily leave any more power in the hands of the administration.

---

10. Fuller, Lon. L., *The Morality of Law* (New Haven: Yale University Press, 2<sup>nd</sup> ed., 1969), cited in Dourado (this volume), n. 6, Walpole and Evans (this volume), n. 11.

11. Dicey, Albert V., *Introduction to the Study of the Law of the Constitution* (London: Macmillan, 1885) (and later editions), cited in Freedman and Vella (this volume), n. 31, Griffiths, Shelley, “Revenue Authority Discretions and the Rule of Law in New Zealand” (this volume), text at nn. 5-6, Dourado (this volume), text at n. 42, Walpole and Evans (this volume), n. 10.

12. Raz, Joseph, *The Authority of Law: Essays on Law and Morality* (Oxford: Clarendon Press, 1979), ch. 11 (“The Rule of Law and its Virtue”), cited in Freedman and Vella (this volume), n. 59, Dourado (this volume), n. 7, Walpole and Evans (this volume), n. 15.

13. Krygier, Martin, “Rule of Law”, in Neil Smelser and Paul Baltes (eds.), *International Encyclopedia of the Social and Behavioral Sciences*, Vol. 20 (Oxford: Elsevier, 2001), cited in Walpole and Evans (this volume), n. 17.

14. United Nations Security Council, “The rule of law and transitional justice in conflict and post-conflict societies”, S/2004/616 (23 August 2004), cited in Mazansky, Ernest, “Revenue Authority Discretions and the Rule of Law: South Africa” (this volume), n. 2.

15. See discussion in Walpole and Evans (this volume), text at nn. 6-8; Dourado (this volume), text at nn. 4-9 and 23-25.

16. See Dourado (this volume), text at nn. 28 and 33-34.

## Contact

IBFD Head Office  
Rietlandpark 301  
1019 DW Amsterdam  
P.O. Box 20237  
1000 HE Amsterdam, The Netherlands  
Tel.: +31-20-554 0100 (GMT+1)  
Fax: +31-20-620 8626  
Email: [info@ibfd.org](mailto:info@ibfd.org)  
Web: [www.ibfd.org](http://www.ibfd.org)



IBFD, Your Portal to Cross-Border Tax Expertise