
Chapter 22

The Classification of Tax Disputes, Human Rights Implications

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22.1. The controversial *Ferrazzini* judgment

On 12 July 2001, in the case of *Ferrazzini v. Italy*, the European Court of Human Rights¹ (ECtHR) reached the following conclusion:

29. [T]he Court considers that tax matters still form part of the hard core of public-authority prerogatives, with the public nature of the relationship between the taxpayer and the community remaining predominant. Bearing in mind that the Convention and its Protocols must be interpreted as a whole, the Court also observes that Article 1 of Protocol No. 1, which concerns the protection of property, reserves the right of States to enact such laws as they deem necessary for the purpose of securing the payment of taxes (see, *mutatis mutandis*, *Gasus Dossier- und Fördertechnik GmbH v. the Netherlands*, judgment of 23 February 1995, Series A no. 306-B, pp. 48-49, § 60). Although the Court does not attach decisive importance to that factor, it does take it into account. It considers that tax disputes fall outside the scope of civil rights and obligations, despite the pecuniary effects which they necessarily produce for the taxpayer.

The case of Giorgio Ferrazzini was a case over a tax assessment which took 14 years to conclude. In essence, Giorgio Ferrazzini argued that the length of the proceedings relating to the determination of the issue had exceeded a “reasonable time” contrary to Art. 6(1) of the European Convention on Human Rights (ECHR). The ECtHR declared the complaint admissible but held, 11 votes to 6, that Art. 6(1) of the ECHR does not apply to tax disputes because tax disputes are not civil rights and obligations to which Art. 6 applies. The decision of the ECtHR in *Ferrazzini* implies that in a tax dispute a litigant does not have a right to a fair hearing under Art. 6 of the ECHR (“the *Ferrazzini* dictum”).²

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1. Application No. 44759/98.

2. A right which enshrines the right of access to court, justice within a reasonable time, right to a public hearing and right to a fair and impartial tribunal.

22.1.2. Perverse conclusion

The conclusions reached by the ECtHR in *Ferrazzini* were heavily criticized. Philip Baker was very vociferous in his criticism.³

The decision in *Ferrazzini* was tainted by a very strong dissenting opinion. In his dissenting opinion, Giovanni Bonello, the Maltese judge, did not mince words. He pointed out that, “2. The Convention does not contain any definition of what is meant by ‘civil rights and obligations’”.

Bonello, who besides being Malta’s leading lawyer on human rights is also a leading historian, studied the historical evolution of Art. 6 and concluded that the *Ferrazzini* dictum was the result of a misreading of the term “civil rights”. He pointed out that,

3. In order to understand the present case-law and the possible need to revise it, it is in my opinion essential to recall the historical background for introducing the concept “civil” into Article 6 § 1 – a concept which is not found in the English text of the corresponding Article 14 of The International Covenant on Civil and Political Rights. Article 8 of the American Convention on Human Rights, on the contrary, expressly covers tax disputes (“rights and obligations of a civil, labour, fiscal or any other nature”).

The travaux préparatoires relating to Article 6 of the Convention – closely linked to those of Article 14 of the Covenant – demonstrate in my opinion the following: (1) it was the intention of the drafters to exclude disputes between individuals and governments on a more general basis mainly owing to difficulties at that time in making a precise division of powers between, on the one hand, administrative bodies exercising discretionary powers and, on the other hand, judicial bodies; (2) no specific reference was made to taxation matters, which are normally not based on a discretion but on the application of more or less precise legal rules; (3) the exclusion of the applicability of Article 6 should be followed by a more detailed study of the problems relating to “the exercise of justice in the relations between individuals and governments”; accordingly, (4) it seems not to have been the intention of the drafters that disputes in the field of administration should be excluded forever from the scope of applicability of Article 6 § 14. Against that background it is understandable that the Convention institutions, in the first years after the Convention came into force, applied Article 6 § 1 under its civil head on a restrictive basis in respect of disputes between individuals and governments. On the other hand, it is hard to accept that the travaux préparatoires, dating more than fifty years

3. Baker, P., “The Decision in *Ferrazzini*: Time to Reconsider The Application of the European Convention on Human Rights to Tax Matters”, available at http://www.taxbar.com/documents/Ferrazzini_Philip_Baker.pdf.

back and partly based on preconditions that have not been fulfilled or are no longer relevant should remain a permanent obstacle to a reasonable development of the case-law concerning the scope of Article 6 – in particular in areas where there is an obvious need to extend the protection granted by that Article to individuals. The present case-law clearly demonstrates in fact that the Convention institutions have not felt bound to maintain a restrictive attitude, but have extended the applicability of Article 6 § 1 to a considerable number of relationships between individuals and governments, which originally must have been held to be excluded.

Bonello proceeded to give a long illustrative list of disputes involving the government where the ECtHR had conceded an application of Art. 6.⁴ Bonello emphasized that in his opinion Art. 6 applied to tax

4. “The following examples could be mentioned to illustrate what disputes between individuals and governments the Court has so far held to be covered by the civil head of Art. 6:

(a) proceedings concerning expropriation, planning decisions, building permits and, more generally, decisions which interfere with the use or the enjoyment of property (see, for example, *Sporrong Lönnroth v. Sweden*, judgment of 23 September 1982, Series A no. 52; *Ettl and Others v. Austria*, *Erkner and Hofbauer v. Austria*, and *Poiss v. Austria*, judgments of 23 April 1987, Series A no. 117; *Håkansson and Stureson v. Sweden*, judgment of 21 February 1990, Series A no. 171-A; and *Mats Jacobsson v. Sweden* and *Skärby v. Sweden*, judgments of 28 June 1990, Series A no. 180-A and B);

(b) proceedings concerning a permit, licence or other act of a public authority, which forms a condition for the legality of a contract between private persons (see, for example, *Ringelsen v. Austria*, judgment of 16 July 1971, Series A no. 13);

(c) proceedings concerning the grant or revocation of a licence by a public authority which is required in order to carry out certain economic activities (see, for example, *Bentham v. the Netherlands*, judgment of 23 October 1985, Series A no. 97; *Pudas v. Sweden*, judgment of 27 October 1987, Series A no. 125-A; *Tre Traktörer AB v. Sweden*, judgment of 7 July 1989, Series A no. 159; and *Fredin v. Sweden* (no. 1), judgment of 18 February 1991, Series A no. 192);

(d) proceedings concerning the cancellation or suspension by a public authority of the right to practise a particular profession, etc. (see, for example, *König v. Germany*, judgment of 28 June 1978, Series A no. 27, and *Diennet v. France*, judgment of 26 September 1995, Series A no. 325-A);

(e) proceedings concerning damages in administrative proceedings (see, for example, *Éditions Périscope v. France*, judgment of 26 March 1992, Series A no. 234-B);

(f) proceedings concerning the obligation to pay contributions to a public security scheme (see, for example, *Feldbrugge v. the Netherlands*, judgment of 29 May 1986, Series A no. 99, and Deumeland, cited above);

(g) proceedings concerning disputes in the context of employment in the civil service, if “a purely economic right” was asserted, for instance the level of salary, and “administrative authorities’ discretionary powers were not in issue” (see, for

disputes because Art. 6 impinged on the pecuniary interests of citizens. He argued that Art. 6 is a procedural guarantee which should apply also in tax disputes,

It is not open to doubt that the obligation to pay taxes directly and substantially affects the pecuniary interests of citizens and that, in a democratic society, taxation (its base, payment and collection as opposed to litigation under budgetary law) is based on the application of legal rules and not on the authorities' discretion. Accordingly, in my view Article 6 should apply to such disputes unless there are special circumstances justifying the conclusion that the obligation to pay taxes should not be considered "civil" under Article 6 § 1 of the Convention.

22.1.3. *Ferrazzini* eroded

The *Ferrazzini* judgment made a lot of noise and was perceived as a controversial decision. However, in reality the undesirable decision in *Ferrazzini* was neither the first nor the last in a long number of similar judgments.⁵ Four years after the ECtHR ruled in *Ferrazzini*, in February 2004, the *Ferrazzini* judgment was confirmed in *Jussila v. Finland*.⁶ The *Ferrazzini* dictum seems to stand on solid ground but the firm ground on which it is supposed to rest on reminds the author of a glacier in an age of global warming. The strength of the despised *Ferrazzini* dictum is melting down. The *Ferrazzini* dictum is being eroded.

instance, *De Santa v. Italy*, judgment of 2 September 1997, Reports of Judgments and Decisions 1997-V). If, on the other hand, "the economic aspect" was dependent on the prior finding of an unlawful act or based on the exercise of discretionary powers, Art. 6 was held not to be applicable (see, for instance, *Spurio v. Italy*, judgment of 2 September 1997, Reports 1997-V). In this respect the case law of the Court has later been changed (see point 6 below on the judgment of 8 December 1999 in *Pellegrin v. France*). It is true, however, – as stressed by the majority – that in other situations the Court has held that Art. 6 is not applicable to disputes between individuals and governments, (see, inter alia, *Pierre-Bloch v. France*, judgment of 21 October 1997, Reports 1997-VI, p. 2223, concerning the right to stand for election, and *Maaouia v. France*, no. 39652/98, ECHR 2000-X, concerning decisions regarding the entry, stay and deportation of aliens).⁷

5. Similar conclusions were reached by ECtHR in the 1960s in *X. v. Belgium* the 1960. By 1973 the ECtHR spoke of *X v. Belgium* as "jurisprudence constant". In 1999 ECtHR expressly held that fundamental human rights do not apply to ordinary tax proceedings (*Vidacar SA and Opergrup SL v. Spain*).

6. Application 00073053/2001. In the case, the Court held that "As regards the tax inspections, the Court notes that it has been established in its case law that tax matters fall outside the scope of civil rights and obligations pursuant to Article 6 of the Convention."⁷

It is important to point out that the purview of the *Ferrazzini* judgment is *ex admisissis* a limited one. The ECtHR felt that it had to emphasize that,

20. The parties having agreed that a "criminal charge" was not in issue, and the Court, for its part, not perceiving any "criminal connotation" in the instant case (see, a contrario, *Bendenoun v. France*, judgment of 24 February 1994, Series A no. 284, p. 20, § 47), it remains to be examined whether the proceedings in question did or did not concern the "determination of civil rights and obligations".

In his dissenting opinion in *Ferrazzini* Judge Bonello commented,

Since *Bendenoun v. France* (judgment of 24 February 1994, Series A no. 284), the Court has consistently considered proceedings relating to tax disputes to be "criminal" if tax fines, surcharges, etc., with a deterrent and punitive purpose are imposed or even if there is a risk that they may be imposed (see, most recently, *J.B. v. Switzerland*, no. 31827/96, ECHR 2001-III). The result is no different if the proceedings also concern the tax assessment as such (see the admissibility decision of 16 May 2000 in *Georgiou v. the United Kingdom*, no. 40042/98, unreported). This implies that the level of protection under Article 6 § 1 of the Convention varies depending on how the legal framework for tax proceedings is organised in the different legal systems; and even within one legal system it may be purely a matter of coincidence whether penalty proceedings and tax assessment proceedings are joined or not. An interpretation of the Convention that leads to such random results is far from satisfactory.

The decision in *Ferrazzini* purports to restrict the application of human rights safeguards to taxation disputes but this does not mean that human rights do not apply to all cases with a tax law element. Classification is key. The nature of a dispute determines the applicability of fundamental human rights to such a dispute. In 1986, the ECtHR held in *Bendenoun v. France*⁷ that a tax case involving penalties was to be considered as a criminal prosecution and Art. 6 applied to it. When a tax dispute is classified either as a dispute of a criminal nature or a dispute of a civil law nature the draconian dictum in *Ferrazzini* does not apply. The *Bendenoun* principle begs the question as to what makes a tax dispute a criminal dispute to which Art. 6 applies.

22.2. The classification of tax disputes; Baker's "Engel criteria"

When is a tax case a pure tax case? When does a pure tax case become either a civil dispute or a criminal case? When does a tax case become a

7. Application No. 12547/86.

determination of civil rights and obligations? An answer to these questions may be drawn from what Baker calls the “*Engel* criteria” developed in the case of *Engel v. Netherlands*.⁸

Baker observed that,

Whether or not proceedings involve the determination of a criminal charge does not depend only upon whether the conduct in issue is regarded by the domestic law of the State concerned as falling within the scope of the criminal law. The term “criminal charge” has an autonomous, Convention meaning. The ECtHR has developed a series of tests for determining whether or not proceedings involve the determination of a criminal charge, sometimes referred to as the “Engel criteria”. These three criteria are:

- (a) the classification of the proceedings in domestic law;
- (b) the nature of the offence; and
- (c) the severity of the penalty which may be imposed.⁹

The ECtHR’s classification of disputes erodes the *Ferrazzini* dictum in a material manner. The ECtHR considers many traditional tax disputes to be criminal disputes. The ECtHR’s idea of a criminal dispute is a very broad one and most tax disputes are treated as “criminal disputes”. It would appear that few disputes are considered to be “pure tax disputes” to which the *Ferrazzini* dictum applies. The ECtHR has been very generous in its interpretation of the third *Engel* criterion. The ECtHR has treated the tax penalty systems of many jurisdictions as consisting in penalties which were severe enough to be considered as criminal charges within the meaning of the ECHR.

22.3. Developments after Baker 2000¹⁰

In 2000, Baker anticipated that in the eyes of the ECtHR, determinations over liability to substantial tax penalties would no longer be considered to be disputes subject to the *Ferrazzini* dictum and that tax disputes over tax surcharges would be governed by Art. 6 guarantees,

8. (1976) 1 EHRR 647.

9. *Id.*, Baker, P., p.28.

10. The leading article on taxation and human rights remains the seminal work by Baker, P., “Taxation And The European Convention on Human Rights”, *British Tax Review* (2000). In the present paper, this article will be referred to as ‘Baker 2000’. Important developments have occurred since Baker 2000. Baker publishes on the subject regularly.

One practical consequence of this decision is likely to be a further extension of the criminal aspects of Art. 6 to tax proceedings. The European Court has already established that the determination of a liability to substantial penalties for incorrectly completed tax returns involves the determination of a criminal charge, and all the criminal guarantees in Art. 6 will then apply. The issue of which tax penalties involve a criminal charge is gradually being clarified. There may also be a tendency in some countries for taxpayers to ask for the determination of their tax liability and the determination of any penalties to be considered at the same court hearing: in those circumstances, the Court has held that it is not possible to separate out the different parts of the proceedings and that Art. 6 applies to the entire proceedings. One of the bizarre consequences of the decision in Ferrazzini is that Art. 6 will apply in those countries where penalties and liability to tax are determined at the same time, but not in those countries where the determinations are separate.

Baker analysed decisions of the ECtHR up to 2000 and concluded that,

It now seems clearly established, therefore, that a tax-geared penalty can entail a criminal charge, and that the issue of liability to penalties of 25% or higher has been regarded as involving the determination of a criminal charge.¹¹

In the eyes of the ECtHR a tax case which involves a tax penalty of 25% of endangered tax or higher is deterrent and punitive and changes the nature of a tax dispute from that of a pure tax dispute subject to the restrictive Ferrazzini dictum to a dispute of criminal law nature subject to Art. 6. The 2007 case of *Paykar Yev Haghtanak Ltd v. Armenia*¹² is a perfect illustration of such a line of thought.

22.4. An illustration of the application of the *Engel* criteria: The case of *Paykar Yev Haghtanak Ltd v. Armenia*¹³

Paykar Yev Haghtanak Ltd was involved in a dispute with the Tax Inspectorate over a tax assessment which included a surcharge. The applicant lost its case but when it tried to appeal to the national court of last instance, its appeal was returned on the grounds that applicant (which was bankrupt) had not paid a court fee. The applicant company complained that it had been unlawfully denied access to the Court of Cassation and that Art. 6 (fair hearing) had been infringed. The point at issue was, in the light of the

11. Id., Baker, P., p. 30.

12. Application No. 21638/03, 20 December 2007.

13. Id.

judgment in *Ferrazzini*, whether Art. 6 applied to the case in point. The issue revolved around a matter of classification. Art. 6 does not apply (in terms of *Ferrazzini*) to pure tax disputes but still applies to disputes over a criminal charge. The crux of the issue was whether the Armenian tax surcharge amounted to “a criminal charge” for the purposes of Art. 6. The ECtHR held that the surcharges attached to the assessment in dispute were deterrent and punitive. Furthermore, penalties were substantial and were up to 43%. The ECtHR concluded that the case in point was not a pure tax dispute subject to the *Ferrazzini* dictum but it was a case over a criminal charge to which all the guarantees of Art. 6 applied. The ECtHR found that applicant had been denied access to Court in violation of Art. 6.

The Court reiterates at the outset that tax disputes fall outside the scope of civil rights and obligations under Article 6, despite the pecuniary effects which they necessarily produce for the taxpayer (see, among other authorities, *Ferrazzini v. Italy* [GC], no. 44759/98, § 29, ECHR 2001 VII). However, when such proceedings involve the imposition of surcharges or fines, then they may, in certain circumstances, attract the guarantees of Article 6 under its “criminal” head. The present case concerns proceedings in which the applicant company was found to be liable to pay profit tax, VAT and simplified tax plus additional surcharges and fines. It remains therefore to be determined whether Article 6 can be applicable to the proceedings in question under its “criminal” limb.

33. The Court reiterates that the concept of “criminal charge” within the meaning of Article 6 is an autonomous one (see *Janosevic*, cited above, § 65). In determining whether an offence qualifies as “criminal”, three criteria are to be applied: the legal classification of the offence in domestic law, the nature of the offence and the degree of severity of the possible penalty (see *Engel and Others v. the Netherlands*.... The second and third criteria are alternative and not necessarily cumulative: for Article 6 to apply by virtue of the words “criminal charge”, it suffices that the offence in question should by its nature be “criminal” from the point of view of the Convention, or should have made the person concerned liable to a sanction which, by its nature and degree of severity, belongs in general to the “criminal” sphere (see *Janosevic*, cited above, § 67). The minor degree of the penalty, in taxation proceedings or otherwise, is not decisive in removing an offence, otherwise criminal by nature, from the scope of Article 6 (see *Jussila*, cited above, § 35, where the Court found Article 6 to be applicable even when the surcharge imposed amounted to only 10 per cent of the tax due).

34. Turning to the first criterion, the surcharges and fines in the present case were imposed in accordance with various tax laws and are not classified as criminal. This is, however, not decisive (*ibid.*, § 37).

35. As regards the second criterion, the Court notes that the relevant provisions of the Law on Taxes and the Law on Value Added Tax are applicable to

all persons – both physical and legal – liable to pay tax and are not directed at a specific group. Furthermore, the surcharges and the fines are not intended as pecuniary compensation for any costs that may have been incurred as a result of the taxpayer's conduct. The purpose pursued by these measures is to exert pressure on taxpayers to comply with their legal obligations and to punish breaches of those obligations. The penalties are thus both deterrent and punitive.

36. The Court considers that the above is sufficient to establish the criminal nature of the offence (ibid., § 38). It would, nevertheless, also point out that in the present case the applicant company had quite substantial penalties imposed on it: the fines ranging from 10 to 50 per cent and the surcharges for the period of delay cumulatively amounting from about 5 to 43 per cent of the tax due.

37. In the light of the above, the Court concludes that the proceedings to which the applicant company was a party can be classified as “criminal” for the purposes of the Convention. It follows that Article 6 applies.

22.5. Recent Finnish cases – One step further

In the cases quoted in Baker 2000 and in the *Paykar Yev Haghtanak Ltd* case mentioned above, the ECtHR concluded that a tax surcharge was a criminal charge because of the amount of the tax surcharge. The ECtHR seems to have given a lot of weight to the fact that the Armenian tax surcharge ran at the rate of 34%. A year later, in two cases decided on the same day, the ECtHR went even a step further. The ECtHR came up with a sweeping statement that tax surcharges are, for the purposes of the ECHR, criminal charges without going into the details of the percentage of the charge imposed.

In the case of *Hannu Lehtinen v. Finland*¹⁴ decided on 22 July 2008, the applicant complained, in the course of a tax dispute involving a tax surcharge, about the refusal of the Finnish Administrative (Tax) Court to hold an oral hearing and to hear testimony from the applicant and three witnesses proposed by him.

The applicant claimed a violation of Art. 6 ECHR (fair hearing) and the ECtHR decided in his favour.

Article 6 is applicable under its criminal head to tax surcharge proceedings (see *Jussila v. Finland*, § 38). Regarding the parties' differing views on the role

14. Application No. 32993/02.

or impact of the taxation procedure as regards criminal proceedings, the Court notes that under Finnish practice the imposition of a tax surcharge does not prevent criminal charges being brought for the same conduct. That is, however, done in separate proceedings before a criminal court.

In view of the Administrative Court's firm conclusion that an oral hearing could be dispensed with, the Court considers that it is not necessary to examine separately whether the rights of the defence were violated by reason of the court's refusal to hear oral evidence.

The ECtHR reached the same conclusion in the case of *Kallio v. Finland*:¹⁵

Article 6 is applicable under its criminal head to tax surcharge proceedings (see *Jussila v. Finland*, cited above, § 38)....

50. In the present case the Administrative Court was called upon to examine the case as regards both the facts and the law. The applicant disputed the facts upon which the imposition of tax surcharges was founded, requesting an oral hearing of witness evidence in order to elucidate the relevant events. The Administrative Court had to make a full assessment of the case. The crucial question concerned the clarification of the facts and the credibility of the statements of the applicant and the four witnesses who had allegedly been involved in the relevant activities. Nevertheless, the Administrative Court decided, without a public hearing, to uphold the decision. The Court finds that, in the circumstances of the present case, the question of the credibility of the written statements could not, as a matter of fair trial, have been properly determined without a direct assessment of the evidence given in person by the applicant and by the witnesses proposed.

51. There has accordingly been a violation of Article 6 § 1 of the Convention as regards the refusal to hold an oral hearing in the Administrative Court.

22.6. Further implications of the classification of tax surcharges as criminal charges

The classification of tax surcharges as penalties of a criminal nature was a major breakthrough. The relevance of such a classification is not restricted to the movement which is gradually eroding the *Ferrazzini* dictum. The ECtHR's treatment of tax surcharges as criminal charges is relevant even in areas which fall outside the strict parameters of tax controversies. The classification of a tax surcharge as a criminal penalty becomes relevant in the context of the presumption of innocence and the non-heritability of criminal charges. A statement made in the ECtHR's decision in the 2007 case of

15. Application No. 40199/02, 22 July 2008.