

TAXPAYERS AND FAIR TRIAL RIGHTS

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The wheels of justice often turn slowly. That was certainly so for Mr Giorgio Ferrazzini, an Italian taxpayer for whom the appeals process in connection with tax assessments raised on him by the Italian tax authorities took over ten years from commencement to conclusion. Aggrieved by the length of the process, Mr Ferrazzini complained to the European Court of Human Rights ('ECtHR') that his right to a fair trial under Article 6 of the European Convention of Human Rights² (ECnHR') had been infringed. Mr Ferrazzini's application gave the ECtHR an opportunity to revisit the question of whether parties to tax disputes are afforded the protection of Article 6 of the ECnHR. They answered this question in the negative. In this article, I shall consider the extent to which a taxpayer may rely upon the rights and freedoms guaranteed by Article 6³ post-*Ferrazzini*.

*Ferrazzini v Italy*⁴ - Summary

Mr Ferrazzini was an Italian citizen, living in Oristano, Italy. He and another person transferred land, property and money to a limited company owned by him. The company's business was organising farm holidays for tourists. It applied to the Italian tax authorities for a tax reduction, and paid the (reduced) sum it considered due.

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² Or to use its full title, The Convention for the Protection of Human Rights and Fundamental Freedoms 1950.

³ This article deals only with the question of whether tax cases are subject to Article 6, and not the actual rights and freedoms protected by it. For a discussion of those rights and freedoms, the reader is referred to the many practitioner texts on Human Rights, but in particular to the excellent 'Law of Human Rights' by Richard Clayton and Hugh Tomlinson, published by *Oxford University Press*.

⁴ Application no. 44759/98, reported in the UK at 2001 [STC] 1314.

Assessments were served on Mr Ferrazzini in respect of IN.V.IM⁵, stamp duty, mortgage registry tax and capital transfer tax⁶ on the basis that the reduced rate did not apply. Mr Ferrazzini sought to challenge the assessments, and commenced the necessary proceedings to do so, at the beginning of 1988. In March 1998, the District Tax Commission informed Mr Ferrazzini that a hearing of his appeal had been listed for 9th May 1998. These appeals were then adjourned in order to enable him to appoint a lawyer, and a hearing was subsequently listed for 24th April 1999.

The District Tax Commission made its decision on 22nd May 1999, depositing the text of the decision at the registry on 16th July 1999. It dismissed Mr Ferrazzini's application on the basis that the property he had transferred to his company⁷ could not be regarded as the normal assets of an agricultural company, and were therefore outside the scope of the reduced rate of tax.

Mr Ferrazzini's complaint under Article 6 was that as the proceedings had taken such a substantial period of time to be resolved,⁸ he had been denied a hearing within a reasonable time, and therefore a fair trial under Article 6, which provides (insofar as is material) as follows:

- "1. In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law"

The ECtHR held, by 11 votes to 6, that Article 6 does not apply to tax cases of the type brought by Mr Ferrazzini as they involve neither a dispute of a 'civil nature' nor a 'criminal charge'.

The Basis of the Decision

As can be seen from the wording of Article 6 set out above, two separate classes of proceedings fall within the ambit of Article 6: disputes involving 'civil rights and

⁵ *Imposta sull'incremento di valore immobiliare*, a capital gains tax.

⁶ *Imposta di registro, ipotecaria e voltura*.

⁷ Which according to the text of the judgment of the ECtHR included a swimming pool and a tennis court.

⁸ Indeed, at the time the matter was heard by the ECtHR in March and June 2001, an appeal against the District Tax Commission's decision (lodged by Mr Ferrazzini in October 2000) remained outstanding.

obligations' and 'criminal charges'. It was accepted in *Ferrazzini* that the case did not involve any criminal charge. The crucial issue was that of whether a tax case involves the determination of civil rights and obligations. There was clearly a dispute between the parties in this matter, however it was not, according to the ECtHR a civil dispute, but a public law matter falling outside Article 6. It held that tax issues remained within the "hard core of public-authority prerogatives" notwithstanding the important pecuniary implications of the case for the taxpayer, with "the public nature of the relationship between the taxpayer and the tax authority remaining predominant"⁹. Mr Ferrazzini had argued that the pecuniary implications for him (or his company) ensured that the dispute was a civil, and not public one.

The Public Law Nature of Tax Disputes

By rejecting the arguments that tax disputes are within the scope of Article 6, the ECtHR's decision was consistent with the earlier decision of *X v France*,¹⁰ in which the European Commission on Human Rights held that an application by a taxpayer who argued that Article 6 had been breached by French legislation which prevented him from adducing evidence which would have undermined the tax assessments raised by the authorities, was inadmissible. *X v France* demonstrated the clear distinction to be drawn for ECtHR purposes between civil and public law matters, and the characterisation of tax disputes as a form of the latter. This decision of the Commission was confirmed by the ECtHR in the case of *Editions Periscope v France*.¹¹

The *Editions Periscope* case is of particular interest in that whilst the ECtHR did re-affirm the principle of inadmissibility of tax cases, the application in that case did actually succeed, due to the way in which it was possible for the applicant's case to be framed. The applicant was a company incorporated in France. Its business was the production of periodicals about new industrial products. Under French law, tax concessions and reduced postal rates were available to the press, and the company applied for these. The authorities refused them on the basis that the periodical in question contained too many advertisements to qualify. Subsequent applications by the company were also refused. In response to this refusal the company sought compensation for discrimination, a claim which the Paris Administrative Court and the Conseil d'Etat both dismissed. The company then alleged that its rights under Article 6 had been infringed. The ECtHR held that the complaint was admissible and that Article 6 had been breached. It justified holding that the complaint was admissible on

⁹ See paragraph 29 of the majority judgment.

¹⁰ (1983) 32 DR 266.

¹¹ (1992) 14 EHRR 597, at para.36.

the basis that although the dispute required it to consider whether the tax concessions had been withheld wrongfully "... the legal basis of the dispute was not the refusal to grant tax concessions as such but the injury occasioned by the allegedly discriminatory attribution of these concessions as between companies competing in the same market."¹²

The distinction drawn in the *Editions Periscope* case is perhaps a somewhat fine one in that both a claim for damages for discrimination (which was admissible under Article 6) and a challenge to the refusal to grant the tax concession (which would almost certainly have been declared inadmissible) arise from the same facts: the refusal of the concession and whilst the pecuniary loss sustained was attributed to the discriminatory conduct of the Tax Authorities, that discriminatory conduct consisted of that wrongful refusal of a tax concession. However, the practical implications of it would seem to be that had the concessions been wrongly refused to all of the applicant's competitors as well, no admissible claim could have been made under Article 6.

A similar approach was adopted in the so-called 'Building Societies cases'¹³ in which several British building societies had paid tax under secondary legislation which was subsequently held to be ultra vires.¹⁴ The building societies brought judicial review proceedings in order to recover the sums overpaid by them, and such claims were stifled by retrospective legislation. The ECtHR held their claims to be within the scope of Article 6, as they were claims for restitution, and not tax cases.

The willingness of the ECtHR to categorise cases between taxpayers and the State as something other than tax cases and therefore capable of protection by Article 6 suggested that there might be scope for a re-appraisal of the decision in *X v France*. Indeed it had been suggested by some leading commentators in the UK¹⁵ that all rights of a pecuniary nature are 'civil' for the purposes of Article 6. This view now seems unsustainable in light of the decision in *Ferrazzini*, in which a similar argument was rejected.

Perhaps most interestingly for the future, in *Ferrazzini* the ECtHR has expressly re-affirmed that the position is susceptible to change in the future. At paragraph 26 of the judgment it states that:

¹² *Ibid.* at para.36.

¹³ *National & Provincial Building Society and Others v UK* (1997) 25 EHRR 127; [1997] STC 1466.

¹⁴ See: *Woolwich Equitable Building Society v IRC* [1992] STC 657.

¹⁵ See: Lord Lester of Herne Hill QC and David Pannick QC 'Human Rights Law and Practice' Butterworths (1999) at para. 4.6.10.

“The Convention is, however, a living instrument to be interpreted in the light of present-day conditions (see, among other authorities, the *Johnston and Others v Ireland* judgment, Series A no. 112 p.25 § 53), and it is incumbent on the Court to review whether, in the light of changed attitudes in society as to the legal protection that falls to be accorded to individuals in their relations with the State, the scope of Article 6 § 1 should not be extended to cover disputes between citizens and public authorities as to the lawfulness under the domestic law of the tax authorities’ decisions.”

Thus, the position as regards the exclusion of tax cases from Article 6 may be subject to change in the future if, in the words of the ECtHR there are ‘changed views in society’. However, given the recent confirmation of the exclusion in *Ferrazzini*, notwithstanding the seemingly more relaxed approach in *Editions Periscope* and the *Building Societies* cases, that change may be a long way off.

Criminal Charges

In *Ferrazzini* the applicant rightly accepted that his case did not involve the determination of a ‘criminal charge’ justifying the application of Article 6. However, in a number of recent cases in the UK, appeals against tax penalties have been categorised as criminal matters for the purposes of the ECnHR, and been afforded the Article 6 rights and protections.

In *Customs & Excise Commissioners v Han and Yau*¹⁶ the taxpayers were restaurant proprietors, who were accused by Customs & Excise (‘Customs’) of under-declaring value added tax (‘VAT’). An assessment for VAT was raised by Customs who also sought to impose penalties under s.60(1) of the Value Added Tax Act 1994, which provides as follows:

“(1) In any case where-

- (a) for the purpose of evading VAT, a person does any act or omits to take any action, and
- (b) his conduct involves dishonesty (whether or not it is such as to give rise to criminal liability),

he shall be liable to a penalty equal to the amount of VAT evaded or, as the case may be sought to be avoided by his conduct”

¹⁶

[2001] EWCA Civ 1040; [2001] STC 1188.

An appeal was brought against the assessment and the penalties, and it was alleged by the appellants that interviews had been carried out unfairly by Customs. The question of whether Article 6 applied was dealt with by way of a preliminary issue. In upholding the VAT tribunal's decision, the Court of Appeal determined that the imposition of a penalty under s.60(1) of the Value Added Tax Act 1994 did involve a criminal charge within Article 6 of the ECnHR. The crucial factors in categorising the penalty as 'criminal' were set out in the judgment of Potter LJ as being (i) the classification of the offence under domestic law; (ii) the nature of the offence; (iii) the nature and degree of severity of the penalty.

Classification of the Offence under Domestic Law

In determining whether a matter is criminal for the purposes of the ECnHR the Court will look at the classification of the offence under domestic law. However, of the three factors set out above, this will be the least important.¹⁷ In *Han and Yau*, the penalty imposed upon the taxpayers was classified as 'civil' for domestic purposes.¹⁸ Notwithstanding this classification the Court held that for ECnHR purposes that penalty was a criminal matter. In treating the domestic categorisation as merely indicative, but not determinative, the English Court acted consistently with the approach of the ECtHR most notably in the case of *Ozturk v Germany*.¹⁹ In *Ozturk* the German authorities had attempted to de-criminalise minor traffic offences, by treating them as 'regulatory' matters. Notwithstanding this reclassification, it was held that for Article 6 purposes the offences were 'criminal'.

As regards the nature of the offence, it is relevant that in order for a s.60 penalty to arise, the taxpayer's conduct must be dishonest. Dishonesty is an element generally regarded as deserving of a criminal sanction, and which would have enabled Customs to have brought a criminal prosecution.

Finally, the nature and the severity of the penalty imposed under s.60 indicated that it was 'criminal' in nature. The combination of the potential severity (up to 100% of the tax at stake) and the punitive and deterrent (as opposed to compensatory) nature of the penalty gave further support to the argument that the penalties are criminal. Customs sought to argue that the absence of imprisonment showed a non-criminal nature of the offence, but this was rejected.

¹⁷ See: *Bendenoun v France* (1994) 18 EHRR 54.

¹⁸ Having been introduced to provide Customs with an alternative to bringing a full-scale criminal prosecution against offending taxpayers.

¹⁹ (1984) 6 EHRR 409, a case relied upon in *Han and Yau*.

In addition to *Han and Yau* the English Courts also dealt with the case of *King v Walden (Inspector of Taxes)*²⁰ in which it was asserted that an appeal against penalties imposed by the Inland Revenue (under s.95 of the Taxes Management Act 1970) was a criminal matter for the purposes of Article 6. Again, the Court²¹ held that Article 6 applied to an appeal against such penalties, on a similar basis to that in *Han and Yau*.²² The judge summed up his reasoning on this point in the following terms:

“In my judgment the system of imposition of penalties for fraudulent or negligent delivery of incorrect returns or statements is ‘criminal’ for the purposes of Art 6(2). I hold so for the following reasons: (a) Plainly the system is intended to punish the defaulting taxpayer and to operate as a deterrent. (b) The amount of the fine is potentially very substantial. (c) The amount of fine is not related to any administrative matter. In particular the fine is not limited to the administrative and other extra cost of dealing with the taxpayer concerned.... (d) The amount of the fine imposed depends on the degree of culpability of the taxpayer, the less culpable the more mitigation there is. Mitigation is an essentially criminal rather than civil consideration. (e) It is accepted that generally ... it is not for the taxpayer to show that the determination of the penalties was wrong. On appeal the burden of proof lies on the Crown.”

Arguably *King v Walden* goes further than *Han and Yau* in that the penalties in the former case imposed under s.95 of the Taxes Management Act 1970 (which were in issue in *King v Walden*) may be imposed where a person has acted “fraudulently or negligently”. In *Han and Yau* Potter LJ relied heavily on the requirement that the penalty under s.60 of the Value Added Tax Act 1994 required dishonest conduct. However, *King v Walden* suggests that dishonesty is not a requirement in establishing the criminal nature of a penalty: a taxpayer acting ‘negligently’ will suffice. Whilst in *Han and Yau* Potter LJ sought to leave this issue open in respect of VAT misdeclaration penalties (which do not require dishonesty),²³ the application of Article 6 to penalties imposed for negligent conduct is certainly not inconsistent with the ECtHR decisions such as *Ozturk v*

²⁰ [2001] STC 822.

²¹ In this case, Jacob J sitting in the High Court, Chancery Division.

²² The High Court appeal in *King v Walden* was decided before the Court of Appeal decision in *Han and Yau*. The two decisions are consistent, and *King v Walden* was referred to with approval in the Court of Appeal in *Han and Yau*; similarly the VAT tribunal decision in *Han and Yau (Han v Customs & Excise Comrs. (2000) ITLR 224)* was referred to in the judgment of Jacob J in *King v Walden*.

²³ [2001] STC 1188 at 1213d.

Germany.²⁴

Whilst the *Han and Yau* and *King v Walden* decisions have caused a degree of excitement in UK tax circles, it is worth noting that to some extent they have merely confirmed the position established by the earlier opinion of the European Commission on Human Rights in *Bendenoun v France*²⁵. In *Bendenoun*, the taxpayer was a French citizen who lived in Zurich, and was a dealer in coins. He formed a limited company under French law, and acted as its chairman and managing director. Three sets of proceedings were brought against him by the French tax authorities as a result of his (and the company's) activities. The taxpayer's complaint in relation to the proceedings was that the Courts had not considered the entirety of the file dealing with customs matters, but had only relied on certain selected parts thereof, and therefore had failed to provide him with a fair trial. The Government argued that Article 6 did not apply to the proceedings in which penalties could be imposed, as they were not criminal, but regulatory or administrative matters. The Commission applied the three criteria later applied by the English Courts in *Han v Yau*, and determined that the cases were criminal.²⁶

The Future?

In the near future there will undoubtedly be further cases in which the Courts will be required to decide whether particular tax penalties are within the scope of Article 6 by virtue of their being criminal. In *Han and Yau* Potter LJ expressly left open the question of whether penalties under s.63 of the Value Added Tax Act are criminal and it is understood that this issue is currently the subject of litigation between taxpayers and UK Customs. In addition, there is the question of which (if any) of the criteria applied in the cases is most important and is likely to require determination in due course. For example, under s.98(1) of the Taxes Management Act 1970, a fixed penalty not exceeding £300 may be imposed for certain failures in compliance – are these 'criminal'? On the one hand, they are punitive and deterrent measures which bear no relation to any administrative costs incurred by the Revenue and subject to mitigation (therefore satisfying criteria (a), (c) and (d) relied on by Jacob J in *King v Walden*, as set above) but are of a relatively trivial amount (thereby failing to satisfy criterion (b)) and do not involve any dishonesty (an important factor in *Han and Yau*). On balance, it would seem likely that the correct answer is that such penalties should be viewed as criminal, as the missing elements referred to did not prevent the penalties at issue in

²⁴ (1984) 6 EHRR 409.

²⁵ (1994) 18 EHRR 54.

²⁶ Although no actual breach of Article 6 was established.

*Ozturk v Germany*²⁷ from being held to be criminal.

In the longer term, it may be (as mentioned in the majority judgment in *Ferrazzini*) that the ECtHR will consider it appropriate to end the exclusion of non-criminal tax appeals from Article 6. Certainly the willingness of 6 judges to publish a dissenting judgment on the question suggests that the answer is perhaps less clear-cut than it once was. However realistically such a change is only likely to take place some considerable way into the future. For the time being, taxpayers will have to be content with having some fair trial rights, but not very many.

²⁷

(1984) 6 EHRR 409.