REPORT ON THE DEVELOPMENTS INTRODUCED IN THE NEW TAX OFFENSE REGULATION: SOME SUGGESTIONS FOR IMPROVEMENT.-

Review of the book sponsored by the Tax and Competitiveness Foundation written by two attorneys from the Cuatrecasas, Goncalves Pereira law firm, one of the firms that make up the Foundation's board of directors (Miro Ayats and Jordi de Juan).-

INTRODUCTION: LEGAL CERTAINTY AS THE DRIVING FORCE OF ECONOMIC DEVELOPMENT.-

Economic progress and legal certainty are two concepts that are inextricably linked. Legal rules must be clear and precise, especially when said rules are the basis for defining areas of coercive action by the public authorities. Only in this way does the legal system become the fertile land where the generation of collective wealth can germinate.

In recent months we have witnessed a cascade of legislative developments that directly affect the economic environment. A large part of these developments are linked to tax law and are aimed at achieving two objectives:

a) Increasing the tax burden, with the objective of reducing public deficit;

b) Increasing the powers and prerogatives of the Tax Administration Agency on the control of taxpayers and the fight against tax fraud.

An integral component of this second objective is the recently adopted reform of what constitutes a tax offense (Organic Law 7/2012 of December 27, BOE 312 of December 28, 2012).

Historically, scientific literature and practical experience have revealed a number of deficiencies in establishing the existence of the grounds for fiscal offense. We note, by way of example only, the problems arising regarding the statute of limitations for criminal liability, distinct from the 4-year limitation period for tax obligations; the changes in jurisprudential course concerning the possible criminal liability for tax fraud, when it was evident that it did not involve penalties in administrative matters; the uncertainty of the offender type that gives rise to the practice of having to regularly seek legal expertise (which continues to be a contradiction "in terminis") or the dysfunctions that are generated by the imposition of penal sentences.

Furthermore, the substantive matter on which the tax offense rests is extremely complex, vague and tenuous, being a high and constant source of litigation, with often contradictory criteria and rulings. This is evidenced by the high volume of economic-administrative claims filed, more than 198,532 in 2010. Another study

that confirms this situation is that prepared by SANTOS PASTOR for the Institute for Fiscal Studies entitled "Analysis of tax conflicts and ways to resolve them", published in December 2004. The study found that in 2003, 3,202,266 tax assessments were ordered, of which 185,031 were appealed (5.8%), including both administrative and judicial appeals. For its part, the General Council of the Judiciary conducted a study with data for the year 2001, which revealed that 26,635 tax-related appeals had been lodged in the contentious-administrative courts.

This situation directly affects Spain's economic competitiveness on an international scale. The same is proved true in the reports from the World Economic Forum which notes that among the 16 most problematic factors for doing business in Spain, the tax level occupies the 5th place and tax regulations the 6th. These extremes are confirmed by the study "Executive summary on big business's perception of the Spanish tax system"[1] in which it was found that 78% of respondents considered that the degree of stability of tax rules is reduced and 76% believe felt that the lack of certainty of the Spanish tax system hinders investment decisions considerably or to a large extent.

It goes without saying that a democratic society must stamp out tax fraud with all legal means available, also with the criminal sanctions for the more serious cases of tax fraud. It is in this direction that the guidelines of penal reform are defined.

However, in this paper, we will try to capture those proposals that, in our view, would improve the current classification of tax offenses, from the threefold perspective of uniting and reconciling the necessary fight against tax fraud, respect for individual rights and freedoms, and the legal certainty which is essential for economic progress.

FINDINGS.-

Based on the outlines of the reform of tax fraud offense, and its tax-legal implications, which cannot escape the critical judgment of the practical jurist, we will establish several systematic findings, to which the proposed improvements are inherent; *lege ferenda* proposals that are based on the study before the reader. In general we can say that:

1. The existence of the grounds of the tax offense as defined in Article 305 of the Spanish Penal Code lack adequate definition of the criminal offense. The

[1] Source: "Executive summary on big business's perception of the Spanish tax system" July 2012, prepared by the Universidad Pontifica de Comillas, Competitiveness.Unit for Research and Social Studies in collaboration with the Tax and Competitiveness Foundation.

predetermination of conduct defined as punishable is essential to establishing the type of criminal offense, especially in openly constructed criminal offenses such as tax fraud, which operates on legal categories predetermined by the Tax Law, and legal concepts which are remarkably vague and elastic. Once again, the criminal legislature has missed an opportunity to take on a better technical refinement of the punishable offense.

2. In the future, it would be desirable that the clear definition of the conduct defined as criminal be based on the description of the offense provided to us by the Tax Penalties Law. Or, alternatively, include *deception* as an element of such conduct. Thus we would move from a tax offense to the offense of tax fraud, which is far more meaningful in describing the protected legal right and accused conduct.

3. In our view, a better and more coherent linkage between the criminal law and tax law is necessary in order to move beyond the existing dichotomies and inconsistencies, a process that must evolve in line with greater acceptance of the tax principles and practices in establishing the existence of the grounds of tax offense, constituting the "ultima ratio" for those more serious actions, within the context of a tax sanction uniqueness.

4. The examples given to us by Comparative Law are characterized by a greater typified definition of the punishable offense. Unlike Comparative Law, in Spain a fiscal offense is regulated by the Spanish Penal Code and not the General Tax Code (German Tax Ordinance, the French General Tax Code, the United States Internal Revenue Code). In the Spanish case, there is a greater disconnection between criminal offense and tax offense and, above all, a greater conceptual vagueness in the determination of the tax fraud that is not defined here.

5. The current tenuous grounds for establishing the existence of this type of crime, in practice, serve as a mere interpretative divergence (for example, on the legal classification of certain businesses, on the interpretation and scope of the provisions on bargaining, or on the boundary between assumptions regarding tax avoidance, conflict in the application of tax law and simulation), resulting in the criminal threshold being exceeded, may give rise to proceedings for tax offenses. Therefore it would seem advisable to introduce into the tax fraud regulation, a clarifying rule to avoid penalizing assumptions, centered on mere interpretative divergences.

6. The possible configuration of voluntary adjustment as a negative element of the type of offense raises the issue of the commission of the offense, to the extent that it would not have been consummated until such time when the

possibility of voluntary adjustment had expired. In our opinion, the solution to this problem arising from the poor configuration of conduct defined as criminal, is adopting the same solution as that of Tax Penalties Law, and understand that the *dies a quo* for the computation of the statute of limitations coincides with the administrative statute, and must be placed at the end of the voluntary period for submission of the tax return.

7. Other issues that arise from the new voluntary adjustment regulation should also be solved according to the principles of the Tax Penalties Law, and the Tax Law in general. For example, when talking about "full recognition and payment of the tax debt," it seems that the full recognition should not exclude the possibility of recourse to Article 120.3 of the LGT (Spain's General Tax Law), but should be limited to accepting the facts without extending to their legal classification for tax purposes. In addition, the demand for payment should not exclude the possibility of postponement and fractioning, and the tax debt to be paid should include only the tax, not surcharges and interests that are not self-assessed by the taxpayer unless subject to administrative settlement. Additionally, the option of voluntary adjustment should be allowed in case of transgression by the tax inspection procedure or undue interruption caused by the inspections, a situation accepted in the tax legislation and that is also recognized in the criminal jurisprudence.

8. The penal reform has missed, once again, the opportunity to eliminate the divergence between the criminal statute of limitations (five years) and tax statute (four years) that leads us inevitably to an irreducible aporia, i.e., once the tax debt statute has expired - and, therefore, the tax debt is nonexistent to the Hacienda Pública (Spain's Treasury) - the tax offense continues to subsist. This could lead to a situation in which there is an offense without a protected legal right, unless it is identified, to a greater or lesser extent, with what one might call the revenue interests of the Treasury. Far from resolving this problem, which is already endemic, our tax offense has been compounded with the amendment of the statute of limitations to ten years for aggravated offenses. In short, we consider it appropriate to establish the identity of the criminal and tax statute of limitations.

9. In connection with the new Article 305 bis of the Penal Code, it would seem reasonable to us, an increase of the penalty for those more serious cases of tax fraud, given the greater criminal culpability and complexity in handling such cases where there are intermediaries, fiduciary elements and foreign territories, but not the side effect of extending the statute of limitation involved, and which likens the tax offense to the more serious criminal conduct worthy of criminal sanction. However, we feel that a greater effort

must be made in defining the conduct defined as aggravated. Note that corporate structures with multiple levels, or the very existence of family group holding companies are common in legal transactions. We therefore feel that the legislature must strive to further refine this aggravated conduct and refer, for example, to the use of "dummy corporations" or fiduciary elements *with the clear aim of concealing the true owner of the taxed goods and rights*".

10. Some cases of aggravation, such as that which depends exclusively on the amount defrauded (600,000 Euros), can occur with relative ease in some tax headings such as corporate income tax, which, coupled with the extreme uncertainty of the punishable offense, can be a considerable legal uncertainty, now subjected to an extended ten year statute of limitations. In future reform, it would be desirable to tackle this issue with a reduced penalty that would avoid such a broad statute. Additionally, and in line with the Tax Penalties Law, punitive aggravation could be established based on economic loss in line with the principle of proportionality, i.e., based on the existing ratio between the amount of income or revenue of the fraudulent person or entity and the liability defrauded.

11. This extension of the statute of limitations for the offense not only further distances the tax statute from the criminal, with the resultant loss of legal certainty that causes the subsistence of the prosecution several years after the extinction of the tax liability by expiry of the statue, but it also hinders the voluntary adjustment that is now considered as a negative element of the offense, and not as a legal grounds for acquittal. This extension of the limitation period is dysfunctional not only concerning the statute of limitations (4 years) but also with respect to other obligations under the law, such as the obligation to retain accounting documents (6 years). Thus, with clear prejudice to the right of defense, the taxpayer may be doomed to criminal prosecution when the commercial, financial or documentary evidence that could serve as the basis for his defense have long disappeared.

12. Moreover, the new paragraph 5 of Article 305 of the Penal Code has opened the door to the ordinary legislator, who appears to have been empowered in this regard by the provisions of the Preliminary Draft of the General Tax Law, allowing the Tax Administration Agency to assess and collect without being required to stop their actions owing to the existence of criminal proceedings. It is therefore a first step towards a new model of tax fraud in which the Tax Administration Agency would be able to assess and collect the debt even though criminal proceedings were initiated, a situation that violates the presumption of innocence. The Tax Administration Agency now recovers, to the detriment of the Criminal Court, the settlement of the

liability in case of commission of a crime, contrary to uniform jurisprudence of the Supreme Court.

13. The criminal court, which does not apply the procedural culture of review and control of the Tax Administration Agency inherent in the contentious court, appears *capite deminutus* in its judicial role, reduced to a single body that ratifies the action taken by the Tax Administration Agency, and is limited to verifying the amount of the defrauded liability, without entering its quantitative determination that, ultimately, it is the civil liability derived from the offense: a civil liability that neither determines nor quantifies, nor controls nor demands. In this new scheme there lies a substantial alteration of the powers of the Tax Administration Agency and the Courts and further decreases the rights of defense.

14. We feel that paragraph 5 of Article 305 of the Penal Code should be removed based on the requirements of the right to the presumption of innocence, the principle of criminal prejudiciality and constitutional separation of powers. This results in a total confusion of powers that grants the Tax Administration Agency executive self-governance of its actions when they are subject to a judicial procedure and are under investigation in criminal proceedings, an area traditionally been removed from the structural and functional prerogative of self-governance.

15. Should that extraordinary and unjustified tax collection authority for the defrauded liability be maintained, while the alleged offense is being heard before the criminal court, this must be addressed during the drafting of the Preliminary Draft of the General Tax Law reform, as it is essential to protecting our civil liberties. In this regard the following would seem desirable: the mandatory notification to the investigating judge of all proceedings of executive collection, allowing the administrative appeal against the settlement and against its executive collection, expanding the grounds for opposition to the enforcement measures including discussion of the origin of the settlement, excluding the various forms of executive surcharge of Article 28 of the General Tax Law, or stop the forced sale of the property seized until such time as the criminal proceedings are resolved by final ruling.

16. A more reasonable alternative to ensure the civil liability arising from the offense, without sacrificing procedural and legal guarantees, would be strengthening the current system of precautionary measures under Article 81 of the General Tax Code, under the necessary court supervision, or, the clear formal distinction between defrauded liability, subject to criminal prejudiciality and the exclusive jurisdiction of the criminal courts, and tax liability.

17. We also protest the extent of the use of the legal proceedings for collection for executive levy of fines and civil liabilities. This possibility, as introduced with the Tenth Additional Provision of the General Tax Law, remains dysfunctional and strange. With respect to civil liability, because it continues to be a Private Law matter that should not be subject to collection proceedings, and with respect to criminal sanctions which due to their ontologically criminal nature, it should be determined that their enforcement corresponds exclusively to the Sentencing Court (article 117.3 of the Spanish Constitution).

18. Finally, and given the severity and rigor with which the tax offense is configured, in aspects as diverse the consummation of the crime, the statute of limitations, the immediate enforceability of the liability without remedy, or the difficulties of adjustment, it would be advisable to use this reform of the General Tax Code to embed in the administrative procedure, in addition to the essential pleading stage prior to referral to crime, a legal guarantee mechanism that clearly discriminates between relevant criminal cases and cases that lack criminal relevance, which should be tried in administrative proceedings.

    From this guarantee-based perspective it would be appropriate to also introduce prior, mandatory and binding report of any collegiate body, with participation of independent experts outside the Tax Administration Agency. The aim is not to hinder the exercise of the criminal action, but to establish a legal filter, a control mechanism of legality that, with guarantees of impartiality and professionalism, that ensures that only those facts or records that really constitute a crime are submitted to criminal jurisdiction, and at the same time, help to decongest the courts of such matters.

19. For the introduction of the ideas and proposals in this study, these could be incorporated into the current reform projects of the Penal Code (Draft Penal Code reform approved by the Council of Ministers of 10-11-2012) and the General Tax Code, if a Preliminary Draft exists. This would allow for a calmer analysis of the different problems analyzed than has occurred in the processing of the Organic Law 7/ 2012. `