

## Legitimacy and validity of tax law in an international context

For a long time, tax law scholars have been discussing questions of legitimacy by reference to formal criteria relating to the democratic character of tax authorities and the procedures surrounding adopting and the implementing domestic tax laws. Some of the debate focused on how detailed and precise tax laws should be, whether governments and tax administrations had a margin of freedom to complement the law, whether vague laws meant legal indeterminacy and discretion, and whether tax courts should always have the last word.<sup>1</sup> Another part of the debate was centred around more substantial questions related to the conformity of tax laws with human rights and fundamental legal-constitutional principles such as the ability to pay and equality principles as well as the need to protect legitimate expectations. Discussions almost exclusively concerned the definition of the competences of parliaments, governments, and their tax administrations as well as courts within one independent state. The debate has now evolved to include an international dimension that we propose to further explore in this editorial and special issue.

### I LEGITIMACY IN TAXES AND THE IMPORTANT ROLE PLAYED BY THE OECD

This change in focus from the national to the international level can be explained by the challenges faced by domestic legislators due to globalization that consequently resulted in greater mobility for companies and individuals and thus new tax planning opportunities. The discussion of common challenges and efforts of coordination in terms of information, transparency, and taxation of cross-border investments among OECD countries appeared to be a solution for tax authorities. The OECD Model Convention from 1992 that introduced a new standard characterized by

periodical and rapid updates of its Commentaries in response to economic developments and changes in taxpayers' behaviour reflects this new approach.

The more recent story is known and has raised controversy. The OECD is no longer just producing soft law at an unprecedented pace; it has even managed to support the adoption of a multilateral convention to implement measures against aggressive tax planning (the MLI).<sup>2</sup> Moreover, it is expanding its influence to non-OECD countries whose interests might significantly diverge from or compete with those of OECD countries. Given that the OECD's action is not merely about assisting countries and their tax authorities in collecting tax revenue but also about allocating tax revenue among states, it is impossible to apply a single standard to all without disregarding some countries' interests over others.

This questions the legitimacy of the OECD as a new tax authority in a globalized world. How legitimate are the solutions proposed by an institution whose composition and decision-making process do not reflect the constitutional principles usually applicable in the legal systems of democratic sovereign states? Beyond the OECD, other legitimacy concerns arise regarding mutual agreement procedures between tax administrations and international arbitration led by independent tax experts. These are gaining momentum due to more aggressive tax administrations and the consequent increase in cases of double taxation.

### 2 LEGITIMACY IN TAXES AND SEPARATION OF POWERS IN THE SOVEREIGN'S STATE SETTING

In the post-World War II setting, the rule of law in taxes, meaning the approval of tax regimes by parliaments, was

#### Notes

<sup>1</sup> Ana Paula Dourado, *General Report – In Search of Validity in Tax Law: The Boundaries Between Creation and Application in a Rule-of Law State*, in *Separation of Powers in Tax Law*, European Association of Tax Law Professors (EATLP) Congress, Santiago de Compostela 17–23 (A. P. Dourado ed., IBFD 2009, 2010); A. P. Dourado, *No Taxation Without Representation in Principles of Law: Function, Status and Impact in EU Tax Law* 10.2–10.4 (C. Brokelind ed., IBFD 2014); A. P. Dourado, *The Delicate Balance: Revenue Authority Discretions and the Rule of Law – Some Thoughts in a Legal Theory and Comparative Perspective*, in *The Delicate Balance – Tax, Discretion and the Rule of Law* 17, at 3 (C. Evans, J. Freedman & R. Krever eds, IBFD 2011).

<sup>2</sup> *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent BEPS*, 2017, <https://www.oecd.org/tax/treaties/multilateral-convention-to-implement-tax-treaty-related-measures-to-prevent-beps.htm>.

reinstated. This is still the situation and it does not imply that governments lack power. In some democratic regimes, parliaments can delegate legislative competence to governments; the understanding is that, when governments emanate from parliaments, they have an almost equivalent democratic legitimacy. Moreover, even when they do not have any legislative competences, they exercise extensive regulatory power that is often equivalent to the role played by governments with legislative competence.<sup>3</sup>

In both cases, parliaments very often enact the basic rules about the tax object, tax subject, and tax rates and authorize governments to approve the detailed tax regimes concerning deductions, allowances, depreciation, amortization, anti-abuse rules, and the like. According to a traditional view, parliaments are meant to be *political* and composed of politicians while governments are meant to be *executive* and search for skilled members. In practice, in many countries, national parliaments have become unable to effectively exercise their constitutional role as a lawmaking authority and tend to limit themselves to approve government-made legislation. Thus, tax laws are primarily written by tax administrations and government cabinets that are in charge of what is referred to as 'technical work'. In reality, this involves genuine political choices, i.e., what type of foreign income should be taxed or how abusive transactions should be defined. This observation is applicable at the national level but also at the international level.

Concerning the international level, it is worth noting that membership to the OECD offers a number of advantages: OECD members benefit from a well-equipped international institution to jointly accomplish this technical work. The OECD provides the setting for its member countries to identify the upcoming tax challenges, discuss potential solutions, dissent from the latter, and introduce reservations in the OECD Model Convention Commentaries. In practice, it should nevertheless be admitted that only a few countries' officials provide substantive input to the technical discussions and even fewer actively participate in the policy solutions or have their voices heard. Moreover, even countries with a strong voice within

international organizations do not usually have adequate procedures to ensure that the political positions expressed therein actually take into account viewpoints of the whole society they are supposed to democratically represent.

### 3 LEGITIMACY AND VALIDITY OF INTERNATIONAL INSTITUTIONS

These observations have led many tax scholars to question the legitimacy of the OECD in contributing to tax law making. In this context, it is important to stress that legitimacy is a complex concept that has been 'used and abused'.<sup>4</sup> Thus, to assess whether the OECD is legitimate, the meaning of legitimacy must be clarified. If it is linked to the role of parliaments and the states' concept of rule of law, it would be required that domestic parliaments were more engaged in making tax laws, including international and EU tax legislation. This could be achieved by requiring more parliamentary hearings on international tax matters in the countries that participate in international fora.

However, there is another angle to the question of the OECD's legitimacy. If equating legitimacy with validity (in Hart's sense), then the assessment of the role of the EU or the OECD in tax law making will necessarily differ. There is no question that EU law is valid in Hart's sense because all publicly known procedural aspects have been followed for its approval and entry into force.<sup>5</sup> Similarly, soft law, including OECD model conventions, commentaries, and reports are valid whenever they are accepted and cited by the tax administrations or tax courts and discussed by taxpayers in their litigation in a specific jurisdiction.<sup>6</sup>

Hart's work distinguishes between law and morals, stressing that the validity of law exists whenever those that apply it consider it as a binding source (customs, for example, can be valid law)<sup>7</sup>; the same reasoning is applicable to soft law and even to other countries' law as it occurs when a court cites court decisions in other jurisdictions. It could thus be claimed that, if OECD-made soft law is accepted by a country's officials – authorities, courts, arbitrators, taxpayers and with no opposition from the parliament – it is also valid and, in that sense,

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<sup>3</sup> Dourado (2009, 2010), *supra* n. 1, at 24–26.

<sup>4</sup> Christopher A. Thomas, *The Uses and Abuses of Legitimacy in International Law*, 34(4) OJLS 729–758 (2014), doi: 10.1093/ojls/gqu008.

<sup>5</sup> H. L. A. Hart, *The Concept of Law* 97–107 and 110 et seq. (Oxford University Press, second ed. 1994); J. Raz, *The Concept of a Legal System – An Introduction to the Theory of Legal System* 197–200 (2d ed., Clarendon Press 1980).

<sup>6</sup> Recognition of soft law by a sovereign state is a different issue from acknowledging international law as law. Hart was skeptical about international law as law on the grounds that (treaty) 'rules presupposed in the very notion of a self-imposed obligation obviously cannot derive their obligatory status from a self-imposed obligation to obey them': *The Concept of Law*, fn. 6, e.g., at 3, 4, 89, 156, 213 et seq.

<sup>7</sup> Hart, *supra* n. 5, at 121.

legitimate. Importantly, this would not mean that those solutions are good and fair.<sup>8</sup> Based on Habermas, one more condition could be added, i.e., to be seen as valid and legitimate, the soft law solutions should express an authentic understanding of the juridical community, its shared values and interests, and a rational choice of strategies and means. Otherwise, they will not be socially accepted.<sup>9</sup>

This special issue discusses these and other dimensions of the concept of legitimacy in taxation. It sheds light on this complex context by bringing together the perspectives of authors belonging to different legal traditions and cultures. Other articles will follow in subsequent issues.

Our ultimate hope is to contribute to the fundamental debate on the democratization of international tax policy in a globalized world.

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<sup>8</sup> Dourado (2011), *supra* n. 1, at 17.

<sup>9</sup> J. Habermas, *Faktizität und Geltung, Beiträge zur Diskurstheorie des Rechts und des demokratischen Rechtsstaats* 192–194 (Suhrkamp Verlag 1992); J. Waldron, *Law and Disagreement* (Oxford University Press 2004 [1999]), Ch. 2.