TAX INFORMATION

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Advising with Value
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2010: THE YEAR OF TAX ARBITRATION?

In light of the ineffectiveness of tax litigation and the increased mistrust of taxpayers in relation to tax decisions, with the decision-makers very often hiding behind mere decisions of form, it is imperative that we weigh up alternative methods for resolving tax disputes, such as mediation, conciliation, and tax arbitration itself, in order to deal with disputes accumulated and arising out of relations between the State and the taxpayer, thus reversing the feeling of injustice in this area. The situation, characterised by proceedings that are held up for years and which eventually expire, if not for the intervention of legislators in relation to successive acts interrupting and suspending proceedings, naturally leads to considerable financial prejudice to public funds. Even worse, this situation leads to an undesirable feeling on the part of citizens that it may be beneficial not to pay taxes merely because of the State's ineffectiveness. All in all, we have poor administration of public monies and a system that doles out real tax injustice and evokes feelings that this must be thwarted.

Notwithstanding noteworthy progress in the use of new technologies for information gathering and data cross-referencing, along with progress in the recruitment of new judges and in the division of the work of the tax courts into various levels of specialisation, these measures take too long to implement or are difficult to put into practice. Furthermore, their purpose is not to bring about the timely resolution of existing important proceedings. So also despite apparent obstacles placed by the constitution impeding the implementation of some of these plans in the area of taxation, it in fact appears to be time to consider alternative solutions that may help to resolve not only the problem of the sluggish tax legal system, but also the problem of the lack of specialisation of the tax courts in matters of increasing complexity, even involving taxpaying citizens in the administration of practical justice and a new attitude towards the legal duty to pay taxes.

The introduction of a legislative authorisation proposal for introducing

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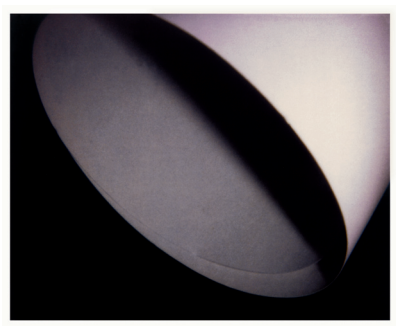
In addition, in the legislative proposal for the 2010 State Budget in the context of alterations to value added tax (VAT), provision is made for the possibility of recovering VAT on debts that are deemed bad, in cases where agreements are reached in extrajudicial conciliation proceedings.

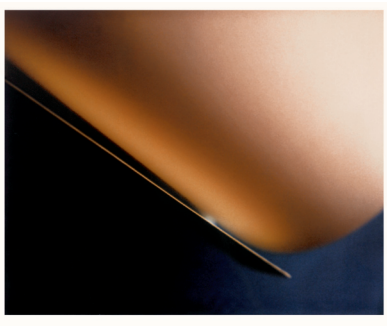
arbitration in the tax domain as an alternative means to the legal resolution of tax disputes was one of the measures deemed worthy of inclusion in the legislative proposal of the 2010 State Budget (http://www.dgo.pt/oe/2010/Proposta/index.htm). The solution was back on the agenda in October 2009 when the Work Group Report for Tax Policy Study was presented (http://www.portugal.gov.pt/pt/Documentos/Governo/MF/Rel_Compet_Efic_Justic_Fiscal.pdf). The conclusions of this report recommended considering alternative ways of resolving tax disputes, including tax arbitration and pre-litigation conciliation commissions. More recently, Councillor Santos Serra supported such a proposal in a written interview in the business newspaper Jornal de Negócios (http://www.jornaldenegocios.pt/index.php?template=SHOWNEWS&id=406235).

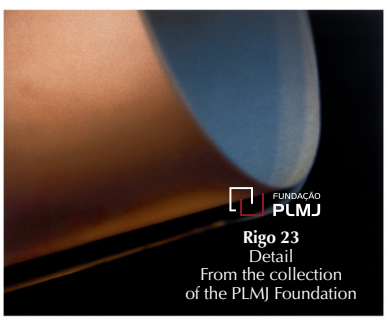
Having acknowledged some of the advantages that arbitration may also bring to tax matters, this legislative authorisation, still to be approved and implemented, will introduce an out-of-court path to the resolution of disputes between taxpayers and the tax authorities. The proposal to establish a provisional six-month period, which may be extended by the same period, for rendering the arbitral decision, the lack of special formalities, and greater specialisation of the arbitrators in the complex matters that they will be called to decide upon, will certainly enable decisions to be made more quickly and will help to clear up pending cases in the courts. This is particularly so since the rules will allow cases currently pending in the tax courts of first instance to be transferred to the arbitration tribunals without the need to pay legal fees, and since the arbitration award will not be subject to appeal. Nevertheless, the legislative authorisation contains a system for challenging the arbitration decision in the courts. Specifically, challenges may be brought on the basis of there being insufficient grounds for the decision, inconsistency in the final decision, and a lacking or excessive judgment, in addition to the possibility to appeal to the Constitutional Court.

So, when instituting the arbitration proceedings, each party must appoint one arbitrator and these arbitrators must then appoint a presiding arbitrator whose independence and exemption will be guaranteed by a strict system of impediment, removal, and substitution. It is expected that the institution of tax arbitration proceedings will have effects similar to those of judicial objection, particularly in terms of suspending the tax enforcement process and interrupting the prescription of tax debts. In addition, recourse to equity will be prohibited, it has been determined that the judgment of the arbitration court be handed down according to existing law. The purpose of tax arbitration proceedings will therefore be to assess, in particular, the legality of tax settlement acts, retentions at source, payments on account, the definition of taxable subject-matter, acts totally or partially dismissing administrative appeals and acts determining equity values. Finally, it is noted that the arbitration decision will have the same enforceability as that attributed to final and non-appealable court rulings.

In addition, in the legislative proposal for the 2010 State Budget in the context of alterations to value added tax (VAT), provision is made for the possibility of recovering VAT on debts that are deemed bad, in cases where agreements are reached in extrajudicial conciliation proceedings. For the purpose of VAT, this broadening of scope brings these conciliation proceedings onto the same level as judicial enforcement and insolvency proceedings and. In effect, by opening up the possibility of VAT recovery on debts that are deemed bad in out-of-court proceedings, there will be a legitimate expectation that this possibility will, in due course, be extended to proceedings subject to tax arbitration and, in fact, since the problem of VAT on bad debts is an issue which significantly impacts the liquidity of companies faced with having to pay VAT to the State without even having received it from their clients, it is appropriate to consider measures that may promote the recovery of this tax.







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Detail
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So with the transposition of the "VAT Package", which has been in force since 1 January 2010, to business-to-business services, outstanding VAT will be self-assessed by the acquirer and recovered according to locally applicable rules.

However, it is also worth pointing out that the VAT system for arbitration services has now been modernised and streamlined with the transposition of directives known as the "VAT Package" (http://www.plmj.com/xms/files/newsletters/2009/Setembro/Novas_Regras_No_IVA.pdf).

The derogation from the general rule on where services are provided which determined that services must be taxed where the service provider has its registered office, has seen a reduction in the administrative charges for entities that resort to arbitration with transnational arbitration services. Under the previous system, entities that incurred foreign VAT when acquiring arbitration services had to undergo a slow and bureaucratic refund procedure.

So with the transposition of the "VAT Package", which has been in force since 1 January 2010, to business-to-business services, outstanding VAT will be self-assessed by the acquirer and recovered according to locally applicable rules. However, from the point of view of the arbitrators, while the "quality/nature" of the acquirer is a determining factor for the purpose of applying the new rules, these arbitrators must obtain the necessary information to determine whether the entity to which services are being provided is registered for VAT and, if so, they must adapt to the new obligations on declarations.

For now, we hope that the bill for the 2010 state budget will be passed in due course.

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06/ 2010