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Specifics of Tax Law Drafting on Selected Issues from the Czech Republic

Szanowny Panie Profesorze,
życzę wszystkiego najlepszego, zdrowia, szczęścia, 100 lat! Dziękuję za inspirację w dziedzinie badań i nauczania prawa podatkowego.

Z poważaniem,
Michal

1. Introduction and several remarks on the method of tax law

While drafting tax law, the legislator should be aware of a specific method of tax law. The general administrative law regulation method is based on the effect of public authorities on the recipients of public authority, in particular by means of the norms enforceable by public authorities and individual administrative acts. The norms are contained in normative administrative acts, i.e., in bylaws and ordinances issued by public authorities, implementing the law within limits stipulated by law (sub-statutory regulations). The individual administrative acts are the decisions of the public authorities authorized by law to make such decisions in the specific administrative matter. Just as public administration is gradually

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absorbing the client model into its operations, where its activities fit the image of real public service in place of the more or less repressive authoritarian police administration of a traditional bureaucratic nature, the administrative law method is also gradually incorporating new elements closer to private law methods (the contract).[2]

The method applied in tax law is essentially a modified version of the administrative law method, namely with regard to the actions of public administration authorities and in relationships regulated by tax law. Statistics can demonstrate a lower level of applying sub-statutory regulations in tax law regulation than in administrative law; in other words, the law gives public administration authorities less space to carry it out. Very few sub-statutory regulations exist in this area; the vast majority of legal regulations in the area of tax law take the form of an act, primarily with regard to such a requirement stipulated in a constitution or a similar document (e.g., in the Czech Republic, such a rule is contained in the Charter of Fundamental Rights and Basic Freedoms,[3] which forms part of the constitutional system along with the Constitution[4]). Of the types of sub-statutory regulations, the most significant in the Czech Republic are the generally binding ordinances, which municipalities (or other local self-government units) use to "complete" the legal regulation of property taxation and local taxes (fees).[5]

Public administration authorities apply economic instruments to a greater extent in the area of tax law to affect recipients. These instruments generally include tax credits and other corrective elements, tax holidays, etc. Certain private law elements also modify the administrative law method (such as the options of lump-sum tax, postponing taxes, payment calendars, etc.) and certain administrative activities are also delegated to private law entities. We can even find typical private law relationships in tax law, such as the relationship of an employer who pays wages or salaries to an employee: their relationship is, without a doubt, a labor law relationship, although the employer is obliged to deduct a personal income tax advance payment as well as social security and health contributions and other levies stipulated by law from the employee's wages, and the employee is obliged to permit such conduct. The authority to withhold tax is thus delegated from the state to a private law entity. Many analogous relationships can be found in tax law (a bank withholds tax on the interest

[2] M. Radvan, *Czech Tax Law*, 4th ed., Masaryk University, Brno 2020, pp. 12–13.

[3] CZ, Charter of Fundamental Rights and Basic Freedoms of 16 December 1992 [*Listina základních práv a svobod*], Act No. 2/1993 Sb.

[4] CZ, Constitution of the Czech Republic of 16 December 1992 [*Ústava České republiky*], Act No. 1/1993 Sb.

[5] M. Radvan, *Czech*…, pp. 12–13.

accrued, a joint-stock company withholds tax on dividends, a seller collects VAT from a buyer along with the sale price, etc.).[6]

What is the most specific to tax law, however, is a principle known as self-application. In tax proceedings (unlike in administrative or financial law), the administrative negotiations do not take place between the administrative authority (tax administrator) and (tax) entity, but, rather, primarily assume the knowledge and orientation of the tax entity in the area of tax law. The taxpayer applies tax law norms to itself by determining the tax base using its knowledge, uses the relevant tax rate for itself, and applies the corrective elements. The taxpayer then delivers the completed tax return to the tax administrator, which assesses the tax tacitly, i.e., implicitly, provided that it has no reservations regarding the correctness and completeness of such a return. In most cases, therefore, there is no interaction at all between the tax administrator and the taxpayer.

We can state that tax law relationships certainly have a public law nature, reflecting the public interest's priorities in the given area. However, the mandatory nature is moderated in certain instances with an element of choice (lump-sum personal income tax, voluntary VAT payer, method of depreciation, lump-sum expenditures for income taxes).[7] Considering the above-stated specifics of the tax law regulation method, the tax law regulation must fulfill very strict quality requirements, respecting the terminology used in other branches of law. The legislator should be receptive to the economic aspects of private and business life. The regulation should not only be perfect but easy to understand and apply, i.e., cheap for both taxpayers and tax administrators.

The following text is dealing with some of the specifics of tax law drafting. It aims to show some problematic issues connected with tax law drafting in the Czech Republic in the last two decades and clarify tax law drafting principles. To achieve the objectives, it is necessary to define tax law drafting principles and sum up if the Czech legislator follows them. In case they are not respected, it would be necessary to give examples and describe and critically analyze the institutes affected by the ignorance of these principles. Based on the research and synthesizing the gained knowledge, this paper will summarize how some tax law drafting principles should be clarified.

While the general tax law principles are often analyzed in detail by most experts dealing with tax law, tax law drafting principles are often disregarded. However, there are outstanding publications by Mastalski,[8]

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[6] *Ibidem*.

[7] *Ibidem*, pp. 13–14.

[8] R. Mastalski, *Wprowadzenie do prawa podatkowego*, C.H. Beck, Warszawa 1995.

Etel,[9] Gomułowicz, and Małecki,[10] or Brzeziński[11] in Poland, Babčák[12] in Slovakia, Mrkývka[13] in the Czech Republic, or Thuronyi in general.[14] One of the essential sources for this paper is the book edited by Nykiel and Sęk[15] on tax legislation standards, trends, and challenges.

2. Principles of tax law drafting

Principles play an important role in the process of tax law drafting and application. They consider both the public interest and tax subjects' individual interests or interests of other tax law addressees. Although many of these principles are not of a normative nature, they allow the postulates of a rational tax system's functioning to be formulated.[16] When drafting the tax law, the legislator is limited by the boundaries of the catalog of basic legal principles given by the Constitution of the Czech Republic, but also by the principles generally valid for continental legal culture and the democratic rule of law. The following text deals with principles legislators should apply in the specific context of tax law drafting.[17]

The principle *nullum tributum sine lege* is the crucial one in the tax law drafting. It is applied by most of the constitutions worldwide. It should be stated that the principle is valid not only for the national acts but for the local bylaw, too. The other constitutional principle *lex retro non agit* means the prohibition of taxation of facts that occurred in the past, i.e., the obligation arising during the effectiveness of a particular regulation is governed by this regulation until its fulfillment. The principle of non-retroactivity might be broken only if the new regulation is advantageous for the obligated tax subject. While drafting the tax law, the legislator

[9] L. Etel (ed.), *System prawa finansowego – Prawo daninowe*, Wolters Kluwer, Warszawa 2010.

[10] A. Gomułowicz, J. Małecki, *Podatki i prawo podatkowe*, LexisNexis, Warszawa 2010.

[11] B. Brzeziński, *Wprowadzenie do prawa podatkowego*, TNOiK, Toruń 2008.

[12] V. Babčák, *Dane a daňové právo na Slovensku*, Epos, Bratislava 2008.

[13] P. Mrkývka, *Determinace a diverzifikace finančního práva*, Masaryk University, Brno 2012.

[14] V. Thuronyi (ed.), *Tax Law Design and Drafting*, International Monetary Fund, Washington 1996.

[15] W. Nykiel, M. Sęk (eds), *Tax Legislation. Standards, Trends and Challenges*, Wolters Kluwer, Warszawa 2015.

[16] L. Etel, *System podatkowy (zarys wykładu)*, WSFiZ, Siedlce 2002, p. 47.

[17] Inspired by Brzeziński (in B. Brzeziński, *Zasady tworzenia prawa finansowego (próba sformulowania)*, "Państwo i Prawo" 1986, No. 5, pp. 66–76) and Nykiel and Sęk (in W. Nykiel, M. Sęk, *Standards, Trends and Challenges of National Tax Legislation*, [in:] *eidem* (eds), *Tax Legislation. Standards, Trends and Challenges*, Wolters Kluwer, Warszawa 2015, pp. 191–206).

should follow the EU law (especially in the field of indirect taxes which are widely harmonized) and international obligations of the state.

Every constitution requires to follow the principle of justice; in the area of tax law, the principle of tax justice. It is applied in two ways, as a horizontal tax justice and vertical tax justice. A horizontal tax justice means that the same objects of taxation should be taxed equally (income, property, or consumption of different persons should be taxed equally regardless of the nature of these persons, their legal status, etc.). A vertical tax justice expresses that an entity with higher incomes, higher valued assets, or higher consumption should pay a higher tax, but not in the sense that the tax rate will increase highly progressively with increasing tax base; the tax rate should remain the same or be progressive proportionally. To the concept of vertical tax justice, the principle of proportionality must therefore be maintained. The related principle of endurance states that the tax must not be of a liquidating nature. The fact that the tax does not have a choking effect is secured by corrective components. These components make it possible to respond to the disproportionate impact of taxes (exemptions, reliefs, etc., or deferral and waiver of the tax by administrative means). It is desirable that there is no double taxation, especially in the interstate tax system. Of course, it is necessary to protect the interests of the majority from the intrusion of different lobby interests.

Other principles are closely connected with the legal system in the country. Primarily, tax provisions should be included in separate legal acts. At the same time, it is necessary to follow a uniform terminology in law. The tax law should not provide tax-specific definitions, but the definitions from other branches of law should be applied, generally even without an express reference.[18] It is inappropriate to impose an unorthodox tax[19] or tax components. The taw law norms must be unambiguous to formulate the addressees' rights and obligations in an understandable and unambiguous form. Ideally, there will be no need to apply any of the contradictory principles *in dubio pro libertate* (*in dubio mitius*) and *in dubio pro fisco*. Concerning the self-application of tax law norms, the tax duties should be formulated briefly and clearly; they should consider the level of legal and economic knowledge of the taxpayers. The title of the legislative instrument must clearly suggest that it concerns tax matters. It is necessary to keep an adequate *vacatio legis* so that the taxpayers have enough time to get acquainted with the new law's content.

As the tax law is closely connected with the national economy, the primal sense of taxation is the fiscal effect for public budgets. This

[18] W. Nykiel, M. Sęk, *Standards, Trends…*, p. 202.

[19] *Ibidem*, p. 203.

principle expresses that the tax must not be an instrument to achieve a purpose other than securing public funds. The tax is not a penalty for earned income, ownership of property, etc. In practice, the principle is often broken as taxes might have reduction and stimulation functions, too. However, the fiscal function must prevail and taxes should not be a tool for politicians to get votes.[20] The tax law drafters should respect the economic rules of a chosen economy model; they should follow the principle of an open market economy. They have to anticipate short-term and long-term consequences of tax law regulation, consider the legal regulation of related sections of public financial activities, limit the impact of fluctuations in the value of money on the stability of tax law, and be aware of the continuity of changes in the amount of taxes.

The last (but not least) tax law drafting principle is that professionals should professionally draft tax law: the proposals of the acts should be consulted with stakeholders, discussed by the professional committees, there should be an adequate explanatory report to the act, etc. I believe that government proposals fulfill most of the standards and follow the principles as described above. However, amendments by members of Parliament seem to be breaking many of these principles. The argument for amendments in the parliamentary procedure is democracy and the legislative power of the Parliament. Interestingly, in the United States (the cradle of democracy), tax bills are sometimes voted under so-called close rules, i.e., a "yes or no vote" without the possibility of introducing amendments.[21]

3. Selected Czech examples of bad practice

Based on the courts' findings, taxpayer and tax offices' experience, it is possible to sum up that the tax law drafting principles are generally followed. Of course, not in all situations. The following observations deal with what appears to be the most critical breaches of tax law drafting principles according to the author's opinion.

Concerning the unorthodox tax components, the Czech legislator was many times very innovative. The most specific tax component in the Czech tax law seems to be the super gross wage as the partial personal income tax base from incomes from dependent activities. The super gross

[20] So-called Christmas tree legislation. *Ibidem*, p. 200.

[21] *Ibidem*, p. 198.

wage was introduced in 2008 with a linear personal income tax rate of 15%. Until the end of 2007, the tax base was defined as income from dependent activity reduced by sums of social security and health contributions paid by the employee (12.5% of the gross income). However, the tax rate was progressive, up to 32%. As the promised tax rate of 15% would have meant a decrease in revenue, it was necessary to increase the tax base. That is why the super gross wage occurred, defined as income from dependent activity increased by sums of social security and health contributions paid by the employer (34%, later 33.8% of the gross income). The personal income tax was then paid not only from income but from other amounts. Moreover, at least social security might be seen as a tax *sensu lato* and being taxed by the income tax, it meant the breach of no double taxation principle.

The other unorthodox tax component might be the tax bonus. Taxpayers with children living in their households have the right to use so-called tax preferences for children: to deduct a fixed amount as the tax reduction. If the tax after this reduction would be in a minus, the tax preference is divided into two parts: tax reduction up to zero tax and tax bonus. If the taxpayer is economically active, the tax bonus should be paid back. It means that some taxpayers not only do not pay the tax, but they get tax from the state.

Mentioning the fixed amounts in tax law, they may breach the principle to limit the impact of fluctuations in the value of money on tax law. It is possible to include both fixed tax rates (e.g., the dog charge rate was changed in 2004 for the last time, while some motor vehicle tax rates have not changed since 1993) and fixed corrective components (especially tax reductions). If fixed amounts are used in tax law, it is necessary to ensure regular amendments.

With regard to the self-application, the tax law norms must be clear, understandable, and unambiguous. The title of the legislative instrument must clearly suggest that it concerns tax matters. However, e.g., the tax on acquisition of immovable property (where the object of taxation was the acquisition of immovable property) was to be paid by the seller and not the acquirer (buyer) for several years. For the proper self-application, the most problematic seems to be corrective elements. In my estimation, the Czech Income Taxes Act[22] includes some 400 corrective components (exemptions, tax reductions, etc.). One third of them might be useful or even necessary (e.g., exemptions of low irregular incomes, reductions for disabled persons, tax preferences for children); the others are to be canceled. However, the legislators are politicians needing votes to be re-elected. One

[22] CZ, Act on Income Taxes of 20 November 1992 [*Zákon o daních z příjmů*], No. 586/1992 Sb., amended.

of the easiest ways to address voters is to grant them tax exemptions (not only before Christmas, as the US experience mentioned above). The Ministry of Finance's newest practice when preparing the new Income Taxes Act is the Christmas tree strategy: the bill sent to the Parliament should have only minimum corrective components (a tree) while the MPs are expected to add a lot of additional ones (to hang decorations on the Christmas tree).

Taxpayers should have adequate time to get acquainted with the new legislation, i.e., the *vacatio legis* must be long enough given the complexity of the new arrangement and the number of changes. *Vacatio legis* differs a lot; there are several examples of good practice from Lithuania and Romania (six months), or Poland, where new income tax regulation must be published by the end of November to take effect on 1 January of the next tax year.[23] In the Czech Republic, the practice is to publish a new tax regulation only several days before starting a new taxable period. For example the amendments to many tax acts effective from the beginning of the tax year 2021 were published only on 31 December 2020.[24]

For the correct tax law interpretation and application, for the understanding of new regulations, the explanatory reports to the acts are beneficial. However, the explanatory reports are often somewhat misleading, especially regarding the reason for changes in tax regulation. Almost every explanatory report to the amendments of excise taxes states that the reason to increase the tax rates is the regulative function of the tax: people will smoke and drink alcohol less if the tax rates are higher and the prices of cigarettes, spirits, beer, and wine are rising. The fiscal function of the excise taxes is being suppressed. During the COVID-19 pandemic, the most popular reason to change (not only the tax) law is the SARS-CoV-2 virus.

The explanatory report is closely connected with the parliamentary procedures and the principles that should be followed in these procedures. The explanatory report is being prepared together with the bill. Both documents are usually prepared by the experts at the Ministry of Finance: legislators and tax professionals. There is an internal comment procedure within the Ministry and an external comment procedure with other ministries and stakeholders. Later, the bill is discussed at the specialized commissions of the Legislative Council of the Government including the commission for financial/tax law, and at the Legislative Council of the Government. After each stage, the explanatory report is specified according to the accepted changes. From this moment, only non-experts (with good exceptions of truly qualified members of Parliament, such as

[23] W. Nykiel, M. Sęk, *Standards, Trends…*, p. 198.

[24] CZ, Act of 22 December 2020 amending certain tax law acts and certain other acts [*Zákon, kterým se mění některé zákony v oblasti daní a některé další zákony*], No. 609/2020 Sb.

Prof. Nykiel) are involved in the legislative processes. The bill is accepted by the Government (still, the explanatory report is further specified if changes are agreed) and sent to the Parliament. Of course, members of Parliament have the right to amend the government bills, but there is no duty to explain the amendments or change the explanatory report. Most of the amendments are never discussed with the Ministry of Finance or any other experts. One of the best illustrative examples is the history of the act amending the tax law acts for the taxable period of 2021. The bill was prepared by the Ministry of Finance and accepted by the Government. However, as a member of Parliament, the Prime Minister prepared his own amendment to this act, canceling the super gross wage as the partial personal income tax base for incomes from dependent activities. The concept of the super gross wage was criticized for many years by many experts. However, I do not believe that the super gross wage should have been abolished this way and during the fiscal crises caused by the COVID-19 pandemic. As the Prime Minister's proposal meant a lower level of taxation, it was accepted. These changes meant the additional loss of public budget revenues in the order of tens of billions of CZK.

4. Conclusions

It is possible to conclude that the tax law drafting principles, as defined by many experts, including Prof. Nykiel, are generally followed in the Czech Republic. However, several cases are showing that this statement cannot be applied in all situations. Nevertheless, the principles' breach was not caused by a lack of principles or their lack of clarity. There is no need to clarify the principles of tax law drafting. To achieve a good quality of tax law, it seems to be enough to follow the principles. The practice should be changed mainly in several areas:

1. Fixed tax rates should be replaced by the percentage tax rates (if possible; probably only if the tax base is replaced, e.g., in the case of property taxes), or there should be specific rules in each act on how the tax rates should be changed with regard to inflation.
2. *Vacatio legis* for tax law must be incorporated, probably directly in the Constitution. In my opinion, three months is an adequate time for the taxpayers, paying agents, and tax administrators to get familiar with new regulations and be prepared for that change, technically and economically. The exceptions might be useful for implementing EU law or in the case of economic, social, or health crises. However, they must not be misused.

3. Theoretically, some tax bills should be voted under so-called close rules, i.e., a "yes or no vote" without the possibility of introducing amendments. Members of Parliament are the only laypeople in the whole legal environment. At the same time, judges, lawyers, notaries, prosecutors, tax advisers, members of legislative committees, etc., must have adequate training, experience, and examination to carry out their activities. I am aware that practically such a rule could never be constitutionalized. Nevertheless, it might become a good practice, and not only in tax law legislation.

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Abstract

The contribution is dealing with some of the specifics of tax law drafting. It aims to show some problematic issues connected with tax law drafting in the Czech Republic in the last two decades and clarify tax law drafting principles. To achieve the objectives, it defines tax law drafting principles and sums up if the Czech legislator follows them. In gives many

examples and describes and critically analyzes the institutes affected by the ignorance of these principles. It is possible to conclude that there is no need to clarify the principles of tax law drafting. To achieve a good quality of tax law, it seems to be enough to follow the principles. The practice should be changed mainly in several areas: 1. Fixed tax rates should be replaced by the percentage tax rates, or there should be specific rules in each act on how the tax rates should be changed with regard to inflation; 2. *Vacatio legis* for tax law must be incorporated, probably directly in the Constitution; 3. Some tax bills should be voted under so-called close rules, i.e., a "yes or no vote" without the possibility of introducing amendments.

Keywords: tax law, tax law drafting, tax law principles