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STATE`S RIGHT TO TAX IN THE LIGHT OF THE EUROPEAN CONVENTION ON HUMAN RIGHTS

Case of EUROMAK METAL DOO v. Republic of Macedonia and Its Impact on the Macedonian Tax Law

Abstract

Tax policy is one of the most important instruments of governments, but it is rarely assessed from a human rights perspective. Traditionally, taxation has been understood as a fundamentally "economic" or "development-related" undertaking by which policymakers generate revenue for socio-economic development. Therefore, fiscal policymakers are concerned with the "economic" aspects of taxation, particularly maximization of tax revenue, rather than non-economic aspects like human rights that, surprisingly, have remained secondary preoccupations. However, this perception has been rapidly changing in the last decade. In circumstances with an increased economic inequality across the world, there is growing recognition that tax policy matters for human rights and has implications for the citizens' enjoyments of these rights, worldwide.

Realizing rights requires resources. In this sense, tax revenue is the most important, the most reliable and the most sustainable instrument to resource human rights in sufficient, equitable and accountable ways. The realization of all human rights, likewise, is a core *raison d'être* of government. It is through respecting, protecting and fulfilling civil, political, economic, social, cultural and environmental rights that the state earns its legitimacy to tax. Moreover, taxes remain the preeminent means through which governments collect revenues necessary to deliver essential public goods and services and to protect rights.

A substantial number of tax cases have gone from national courts to the European Court of Human Rights in Strasbourg. These applications are mostly based on Article 1 (protection of property) of Protocol No. 1 to the Convention, which recognizes that a State is entitled "to enforce such laws as it deems necessary … to secure the payment of taxes or other contributions", and Article 6 (right to a fair trial) of the Convention. One of the tax cases that have been ruled by the European Court of Human Rights is the case of "EUROMAK METAL DOO v. REPUBLIC OF MACEDONIA". In this case, the Court unanimously held that there had been a violation of Article 1 of Protocol No.1 to the European Convention on Human Rights (Protection of property). This paper will focus on legal analysis on this judgment and its impact on Macedonian tax law.

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Keywords: tax sovereign, taxation, taxpayers` rights, value-added tax, protection of property.

I. INTRODUCTION

Taxation has traditionally been understood as a fundamentally "economic" or "development-related" task by which policymakers generate revenue for socio-economic development. Primarily, therefore, fiscal policymakers are concerned with the "economic" aspects of taxation, i.e. maximization of tax revenue, rather than non-economic aspects like human rights and it is hardly surprising that the human rights perspective has remained secondary preoccupations. From this traditional perspective, therefore, it is normally considered that country`s tax system does not violate human rights. Indeed, except for the right to freedom from arbitrary deprivation of property and the right to privacy, it may be difficult to conceive of a right that is threatened (at least directly) by the lawful levying of taxes. Countries` economic development is inextricably intertwined with the enjoyment of human rights and development frameworks that purposively engage with human rights questions are more effective in terms of promoting socio-economic rights and obligations.

The traditional perception of human rights as a narrow set of prescriptions with little or no connection to taxation changes, therefore, when viewed within the wider context of the link between human rights and development. A fiscal framework that incorporates a human rights perspective takes a particularly broad view of the concept of the right, one that extends beyond the narrow 'traditional' approach of rights as spelt out in the international documents, to include a wider spectrum of rights implicated by the design and implementation of fiscal law and policy meant not only to protect the rights of the people but also to promote them.

Human rights principles have a major impact on tax policy by interfering in countries` autonomy in how to impose taxes on individuals and legal entities due to the fact that countries have undertaken certain international obligations regarding promotion and protection of individual rights and obligations. Additionally, human rights principles address more explicitly countries` responsibility to consider how their tax policies and solutions contribute to the problems of global poverty and economic inequity. But, it is equally clear that the realization of human rights depends on laws that regulate the allocation of resources within the society. Countries have an important role in moderating this resource`s allocation. Taxation is a significant mechanism for fulfilling that role. While taxation is primarily seen as a pragmatic mean to collect revenues for government functions, taxes surely enable allocation and redistribution of resources (Christians, 2009).

The application of human rights principles to the tax policy discourse seems not only reasonable but also necessary in light of the restrictions of the country`s tax sovereign. This paper focuses on legal analysis on the judgment of the European Court of Human Rights in the case of "EUROMAK METAL DOO v. REPUBLIC OF MACEDONIA", as one of the few tax cases that have been ruled by the European Court of Human Rights. The added value of the paper will be the author`s recommendations for better and lawful enforcement of Macedonian tax laws in practice with great respect of tax payers` rights vis-à-vis the Court`s decision.

II. STATE`S RIGHT TO TAX VERSUS PROTECTION OF HUMAN RIGHTS: DELICATE BALANCE

There was a time when mentioning taxation and human rights in the same sentence caused a reaction of astonishment. The perception was that human rights were concerned only with problems such as torture, extra-judicial executions and forced labour, rather than with taxation. Not surprisingly, for a long period of time, tax policy was rarely assessed from a human rights perspective. But there is growing recognition that tax policy is a human rights issue, and has implications for the citizens` enjoyments of these rights, both in developed and in developing countries.

Under core human rights treaties, countries acting individually and collectively are obligated to mobilize and allocate the maximum available resources for the progressive realization of civil, political-economic, social and cultural rights. In addition, every country is responsible for mobilizing the resources necessary to implement its international obligation to promote, protect, and fulfil human rights.

Most certainly, fiscal policy can generally make a significant contribution to realizing human rights. In modern circumstances tax policy can only be perceived as the human right policy for three reasons. First, taxation allows countries to raise revenue to finance public goods and services required for the realization of human rights. Second, it can contribute to a redistribution of income and assets from the richer to the poorer strata of society, thus promoting the realization of their human rights. The impacts on the reduction of inequalities and, therefore, on the effective enjoyment of human rights, can therefore be significant (De Schutter, 2017). And finally, with certain goods and services, it can contribute to internalization of their ecological and social costs and thus counteract conduct detrimental to human rights (Obenland, 2013).

Tax revenue is the most important, the most reliable and the most sustainable instrument to resource human rights in sufficient, equitable and accountable ways. The realization of all human rights, likewise, is a core *raison d'être* of government. It is through respecting, protecting and fulfilling civil, political, economic, social, cultural and environmental rights that the state earns its legitimacy to tax. Taxation also plays a fundamental role in redistributing resources in ways that can prevent and redress gender, economic and other inequalities and reduce the disparities in human rights enjoyment that flow from them. Moreover, a just system of taxation can cement the bonds of accountability between the state and its people, fostering governments to be more responsive to the rights and claims of those to whom they are answerable. Tax policies can likewise counteract glaring market failures and protect global common goods – not least a healthy environment within planetary boundaries. Taxes are not the only source of government revenue, but they are arguably the most important, because they combine three critical functions, addressed below: (a) the generation of revenue for the realization of rights; (b) achieving equality and tackling discrimination; and (c) strengthening governance and accountability (Sepulveda, 2014).

Yet many countries struggle to collect sufficient tax revenue to adequately fund the realization of human rights, all of which come with some financial cost. In parallel, unjust tax systems at the national and global levels continue to fuel rising inequality and widening disparities in human rights enjoyment, shifting the burden of financing public services onto society´s least well-off, weakening the provision of existing services and concentrating wealth in the hands of a privileged few. Regressive fiscal policies being pursued in many countries across the globe from North to South are a serious threat to the economic and social rights of already disadvantaged groups. This basic injustice is fuelling deeper economic, gender, and political inequalities, eroding trust in government institutions, which are perceived as more accountable to transnational economic elites than to their people (Lima Declaration on Tax Justice and Human Rights, 2015).

Tax policy is public policy, and so can no longer be treated as a matter of mere technical engineering or be left entirely to the often unaccountable discretion of the government. Instead, governments have to cultivate transformative social and fiscal compacts and empower citizen watchdog institutions that have the purpose of subjecting tax policy to the most rigorous standards of transparency, public participation, and meaningful accountability in line with internationally recognized human rights principles. According to the human rights perspective, policymakers have to take into account a number of determinants in creating and implementing the tax system. Mainly, this so-called "rights-based approach" requires a tax policy that would avoid any direct violation of rights and tax regime which would be specifically designed to promote human rights. Furthermore, establishing a tax system based on this rights-based approach entails few principles, most notably transparency, participation and accountability. As a result, the tax system must be open and transparent as a guarantee to full and timely information regarding the design and implementation of tax law and tax policy. The tax system should enable proactive participation of the public during the creation, introduction and implementation of tax norms and last, but not at least, the tax system should secure accountability.

Existing human rights standards provide a normative justification for a capable and well-resourced state. To comply with their obligations to protect and progressively realize economic and social rights, states must use and generate the maximum available resources (especially through sufficient and sustainable taxation) in equitable, non-discriminatory ways.

The development of tax and fiscal policy must be grounded in the principles of human rights. Greater coherence across government institutions is necessary to ensure that fiscal policies comply with our human rights obligations under international law and do not promote inequitable growth or contributes to further marginalization of people and communities or to creating greater inequality between citizens.

III. APPLICATION OF THE EUROPEAN CONVENTION ON HUMAN RIGHTS ON TAX MATTERS

A number of applicants rely on the European Convention on Human Rights to challenge the rules and procedures of the Contracting States in tax matters and the methods used by tax-authority officials (European Court of Human Rights, 2019).

There are few articles of the Convention and protocols which are more relevant to taxation: Article 1 of the First Protocol (protection of property), Article 6 (right to a fair trial) and Article 14 (prohibition of discrimination). Articles that are of less relevance to taxation are: Article 8 (right to respect for private and family life), Article 9 (freedom of thought, conscience and religion) and various miscellaneous Articles.

When we analyze the Court jurisprudence in tax matters, Article 1 of the First Protocol (protection of property) is the most discussed one, not because it has been raised in the largest

number of cases (that honour belongs to Article 6) but because it is the only Article which makes express reference to taxation (Baker, 2000). This Article protects the enjoyment of property. All taxation is a prima facie interference with the right to enjoy the property, but the second paragraph of Article 1/1 provides a specific exception for taxation. As an exception to a fundamental right, taxation is subject to supervision by the Strasbourg organs to ensure that all taxation must satisfy the principles underlying the Convention: it must be imposed according to law, it must serve a valid purpose in the public or general interest, and the provisions adopted must be a reasonable and proportionate means to achieve that end.
Article 6 provides a basket of guarantees associated with the fair trial of civil and criminal cases. There is established jurisprudence of the Strasbourg organs that ordinary tax proceedings do not fall within Article 6 since they involve public law issues. There are exceptions, however, where proceedings can properly be characterized as involving the determination of "civil rights and obligations" or of "any criminal charge". A substantial number of cases in the Court database have been held to fall within these exceptions, especially where the dispute involved liability to substantial, tax-geared penalties.
Article 14 prohibits discrimination in the enjoyment of the rights protected by the Convention. In a tax context, this Article is most frequently raised in conjunction with Article 1/1. It has been successfully raised primarily in connection with substantive tax rules which apply on a discriminatory basis between men and women.
Article 8 (right to respect for private and family life) may apply both to substantive tax rules and procedural matters. Most cases have raised Article 8 in connection with information-seeking activities of revenue authorities. Taxpayers have been successful where the powers are broad and are not accompanied by adequate judicial safeguards.
So far as Article 9 (freedom of thought, conscience and religion) and other miscellaneous Articles are concerned, complaints under these Articles have almost invariably failed.
Decisions of the European Court of Human Rights are not binding precedents: it is only necessary that they should be taken into account, so far as they are relevant to the proceedings. Neither body has itself adopted a doctrine of binding precedent. In particular, a dynamic approach to interpretation must be adopted to give effect to the Convention which "is a living instrument which … must be interpreted in the light of present-day conditions" (Baker, 2000).

IV. LEGAL ANALYSIS ON THE JUDGMENT OF THE EUROPEAN COURT OF HUMAN RIGHTS IN THE CASE OF "EUROMAK METAL DOO V. REPUBLIC OF MACEDONIA"

This analysis refers to the judgment in the case of "EUROMAK METAL DOO v. REPUBLIC OF MACEDONIA", that the European Court of Human Rights (hereafter "the Court") delivered in favour of the applicant company at the session on 22.5.2018. In this case, the Court unanimously held that there had been a violation of Article 1 of Protocol No.1 to the European Convention on Human Rights (Protection of property).
The case originated in an application against the Republic of Macedonia lodged with the Court by the company EUROMAK METAL DOO (hereafter "the applicant company"), a family business that traded in scrap metal. The applicant company was represented by Mr Igor Spirovski, a lawyer from Skopje.

In this case, the applicant company complained that it had been ordered to pay, with interest, a value-added tax that had previously deducted from its tax obligations. Following the audit in 2009, the Public Revenue Office brought a tax assessment, establishing that the applicant company had made errors in calculating its VAT deductions on received goods because some of its suppliers had failed to declare or pay tax to the State. As a result, the applicant company could not receive a VAT refund, as it had done in the past. Later on, these findings and conclusions of the tax authorities were upheld by the Macedonian Ministry of Finance and the administrative courts.

Relying on Article 1 of Protocol No.1, the applicant company complained that, although it had timely and fully complied with its own obligation as VAT taxpayer according to the Law on Value Added Tax[1], the Macedonian tax authorities had deprived it of its right to deduct the input VAT, because its suppliers had failed to meet their own VAT obligations – circumstances beyond the applicant company`s control.

i. Facts of the case

The applicant company was set up in 1998 as a limited liability company, owned by the married couple Ms. Zhaneta and Mr. Rashko Pavlovski. It traded in scrap metal and for that purpose, it purchased waste aluminium, copper, iron and other metals, processed them and then sold the product.

The applicant company was registered as a taxpayer for VAT purposes and timely and fully completed all VAT obligations (declaring VAT in all issued invoices, fulfilling VAT returns and requesting VAT deductions according to the tax credit method).

During October – November 2009, the applicant company was subjected to a tax audit by the Public Revenue Office, examining the period from 1.1.2005 – 30.6.2009. On November the 6th 2009, the tax authorities brought a tax assessment finding that, due to previous audits in some of the applicant company's suppliers, registered as VAT taxpayers, they had not declared or paid VAT to the State, although it was declared in the invoices issued to the applicant company. Additionally, the audit established that some of the invoices did not contain the suppliers` addresses. And finally, the audit found that the applicant company had paid all the invoices received from the suppliers and that it had declared VAT in all issued invoices. Regarding all issues related to the suppliers, the tax authorities concluded that the applicant company had failed to fulfil all requirements to have the right on VAT deductions, according to the Law on VAT, article 33 and 34.

Based on the tax audit, the applicant company was ordered to pay an additional amount of 3,827,546 Macedonian denars, including interest, as VAT to the State because in the period that was examined it had wrongly calculated the VAT deductions. On March 22nd 2010, the Public Revenue Office issued a written reprimand, ordering the applicant company to pay the amount of 6,050,124 denars (the full amount plus the interest).

The applicant company had appealed the decision, at first to the Ministry of finance, and after that, the applicant company lodged two appeals to the administrative courts. The Higher Administrative Court dismissed the appeal and stated that the applicant company failed to fulfil the cumulative conditions, given in article 33 and 34 of the Law on VAT, to obtain the VAT

[1] Official Gazette of Republic of Macedonia, no. 44/99, 59/99, 86/99, 11/00, 8/01, 21/03, 19/04, 33/06, 45/06, 101/06, 114/07, 103/08, 114/09, 133/09, 95/10, 102/10, 24/11, 135/11, 155/12, 12/14, 112/14, 130/14, 15/15, 129/15, 225/15, 23/16, 189/16, 198/18, 98/19 , 124/19, 275/19 and 267/20.

deductions because some of its suppliers did not declare or pay the VAT to the State. Furthermore, the Court reiterated that it was the applicant company`s obligation to choose its business partners carefully and, in this sense, it should bear the responsibility. Meanwhile, the Public Prosecutor`s Office for Prosecuting Organized Crime and Corruption filed an indictment against several individuals, who were the applicant company`s suppliers, for abuse of service and tax evasion. It was alleged that they used the companies to issue false invoices which were not a result of real commercial activity. However, the companies, as legal entities, were not indicted.
In February 2017, the applicant company was removed from the Central Register of companies, because it had not submitted an annual financial report for 2014, and ceased to exist. At that time, the applicant company`s bank account was blocked by the Public Revenue Office, but due to lack of money, the tax authorities did not succeed to collect any money as VAT.
In 2014, the applicant company lodged an application with the Court under Article 1 of Protocol No.1[2]. The applicant company complained that it had a legitimate expectation with regard to its right to obtain VAT deductions, but, due to circumstances beyond its control, its right of peaceful enjoyment of his possessions was violated by the State.

ii. Judgment

Proceeding in this case, the Court declared that the application: (1) was not manifestly ill-founded and (2) was admissible.

(1) Deciding on the admissibility, the Court rejected the Government objection, stating that the applicant company existed at the time the application was introduced and that its founders and sole shareholders had a legitimate interest in obtaining a final decision of the case by the Court. Additionally, the Court concluded that the applicant company, by appealing against the tax assessment before the domestic tax authorities and the administrative courts, used all available domestic legal remedies in respect of the submitted complaint to the Court.

(2) The Court found a violation of Article 1 of Protocol No.1 to the European Convention on Human Rights. As the State`s interferences, in this case, was clearly "*necessary to secure the payment of taxes*", the Court reiterated that *although the State has a wide margin of appreciation in the field of taxation, an instance of interference must strike a "fair balance" between the demands of the general interest of the community and the requirements of the protection of the individual`s fundamental rights.*

The Court noted that there was no doubt that the <u>applicant company had the right to obtain VAT deductions</u> amounted to at least a legitimate expectation of obtaining an effective enjoyment of the property right. Moreover, the Court observed that the applicant <u>company timely and fully fulfilled its own VAT obligations according to the Law; that it was not alleged that it had participated in any criminal activity, nor it</u>

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[2] Article 1 of Protocol No.1 (**Protection of property):**
(1) Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.
(2) The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.

had or could have had knowledge of whether its suppliers had completed their tax obligations. The Court found that the applicant company should not have been required to bear the full consequences of its suppliers` mistakes by being refused to have a right on VAT deductions and being ordered to pay the VAT again plus interest. Regarding the payment required by the State, the Court considered that it imposed an excessive individual burden on the applicant company which breaches the principle of a fair balance between the demands of the general interest of the community and the requirements of the protection of the right of property. And finally, the Court considered that the State should pay to the applicant company an award of EUR 4,000 as non-pecuniary damage and the amount of EUR 1,500 covering costs and expenses.

V. FINAL REMARKS AND RECOMMENDATIONS

The most significant characteristic of the Value Added Tax is the self-control mechanism, which enables this tax to be the most difficult for tax evasion. In this sense, taxpayers control each other in the process of purchasing and selling products. They are motivated to beware whether their predecessor, in the process of production, sales or distribution, has calculated and declined the VAT in the invoices issued. The record and documentation constitute the *conditio sine qua non* for easy functioning of VAT. As a result, taxpayers acquire the right to deduct the previously paid VAT, according to the tax credit method as the most vital element of this tax.
According to the current tax legislation of the Republic of North Macedonia, which is mostly harmonized with the EU VAT legislation, the right to deduct previously paid VAT **is not obtained automatically, but if the following conditions are met cumulatively: (1) if the taxpayer purchases or imports goods for his commercial activity, and (2) based on invoices issued where the paid tax is separately stated, and these invoices are recorded in the taxpayer's accounting**. This confirms the applicant-company claimants that, having fulfilled the conditions prescribed by the Law, it had a legitimate right to claim and receive the VAT refund, and that it did not violate the Law by any means, which, on the other hand, was confirmed through the long-standing work of the company and in the explanation given in the tax assessment by the Macedonian tax authorities.
Furthermore, fulfilment of the VAT obligations by the taxpayers – suppliers are not prescribed by the Law on VAT as a condition for obtaining the right to deduct the input VAT. Still, this was the main argument for the sanction in the tax assessment imposed by the Macedonian Public Revenue Office.
The Court, with this judgment, has once again confirmed the principle that **one conscientious VAT taxpayer who timely and fully fulfil all legal obligations, has the right to deduct the input VAT, according to the so-called tax credit method, that cannot be conditioned with the actions of the other taxpayers in the VAT system**. A taxpayer cannot be responsible whether his suppliers have declared or paid the VAT to the State. In fact, the Public Revenue Office is the competent and responsible authority, both for determining and collecting taxes, as well as for controlling taxpayers for compliance with tax rules and regulations and fulfilling their legal VAT obligations.

On the other hand, this judgment has significant importance for other companies - registered VAT payers for tax purposes, guaranteeing *legal certainty* in obtaining the right to deduction of the previously paid VAT, in terms when they have fulfilled all their tax obligations to the State.
And finally, in tax sense, this judgment is fair, proportional and justified. In future, in the procedure of determination and collection of taxes, the Macedonia tax authorities and administrative courts should take into account the application of the *principle of fairness and equity in taxation*. Taxation, in any case, should not be an excessive burden to the taxpayer.

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