Petr Mrkývka, Jolanta Gliniecka,
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THE FINANCIAL LAW TOWARDS CHALLENGES OF THE XXI CENTURY

Conference Proceedings

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(Conference Proceedings)

Petr Mrkývka, Jolanta Gliniecka, Eva Tomášková,
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Preface

This publication is a result of long-lasting cooperation between many entities, universities, departments of law and financial law from several countries and many years of their experience. It is a direct result of the 5th edition of the research project called "Financial Law towards Challenges of the XXI century" carried out by "The Gdansk University Center for Self-Government and Financial Law" (hereinafter – the Center), and the Department of Financial Law, Faculty of Law and Administration, University of Gdańsk. The research project resulted in two main outcomes; the organisation of the 5th International Baltic Conference on Financial Law and the 1st International Seminar of Financial Law which was organised by the Centre's scientific magazine Financial Law Review. Both events took place during a cruise across the Baltic Sea and on the Swedish island of Öland on 10–13 May 2019. They brought together more than 100 scientists from 7 participating countries.

The conference was co-organised by the Center, the Department of Financial Law, Faculty of Law and Administration, University of Gdańsk, and the Department of Financial Law and Economics, Faculty of Law, Masaryk University in Brno. The cooperation of both departments has been ongoing for several years. On 24 November 2015, they signed a cooperation agreement. The Law faculties of both universities signed a similar agreement of broader scope as well. Since then, their cooperation has intensified and gradually evolved.

The Gdansk University Center for Self-Government and Financial Law, is a non-departmental unit of the University of Gdańsk and has a seat at the Faculty of Law and Administration. It aims its activities at the integration of society and meeting the needs of non-academic communities. It carries out its programme objectives related to self-government law, especially the local finance law, as well as tasks related to the entire field of public finance and finance law.

The main objective of the Center is primarily the realisation of its projects. It also develops projects in cooperation with other academic and non-academic partners, public and private institutions, local self-government units, non-governmental organisations and others, whose aims are coherent

with the aims of the Center. The Center cooperates with domestic and foreign scientific and didactic institutions, offers specialist courses and lectures on self-government law and local financial law. It participates in the organisation of scientific and research meetings promoting scientific research as well as consulting services. One of the essential forms of the Center's activity is initiating and supporting various publishing undertakings which integrate the scientific society. It has already organised several international scientific conferences and seminars, moreover, issued many publications – mostly of an international character. The Center is also the publisher of the Financial Law Review academic quarter (FLR), which is a scientific magazine published in English in electronic form. The Center also carries out research projects such as "The Financial Law towards Challenges of the XXI Century" and "Local Goventment 21" which focuses on local local-government finances.

The leading partner and the initiator of the Center is the Chair of Financial Law at the Faculty of Law and Administration, University of Gdańsk. Every activity of the Center is primarily realised in cooperation with the Chair and faculty's research workers. The Chair of Financial Law introduced the idea of the research project "Financial Law towards Challenges of the XXI Century" and organised the first conference. The Center took over this idea and continued with subsequent editions, including the creation of "Local Government 21" project.

Over time, other institutions started cooperating with the Center. First, the Faculty of Law and Administration, Cardinal Stefan Wyszyński University in Warsaw, then the Chair of Financial Law at the Faculty of Law, Masaryk University, Brno (Czech Republic) and the Department of Financial Law at the Faculty of Law of the University of Paweł Józef Šafárik in Košice (Slovakia). Constant cooperation with the self-government and governmental administration, in particular with the Regional Chamber of Audit in Gdańsk, significantly raises the substantive level of research projects and publications and also strengthens the practical aspect of research.

Together with the Chair of Financial Law at the Faculty of Law and Administration, University of Gdańsk and with some or all of the previously mentioned partners as well as numerous NGOs, the Center has already

realised eight research projects so far. They resulted in 13 international conferences and international seminars that supplemented or extended topics of the conferences:

- I International Baltic Conference on Financial Law: "The Financial Law towards Challenges of the XXI Century", Gdańsk – Nynäshamn – Stockholm, 8–11 October 2010;
- II International Baltic Conference on Financial Law: "The Financial Law towards Challenges of the XXI Century", Gdańsk – Nynäshamn – Stockholm – Gdańsk, 19–22 April 2013;
- III International Baltic Conference on Financial Law: "The Financial Law towards Challenges of the XXI Century", Gdynia – Karlskrona-Gdynia, 24–27 April 2015;
- Международный научный семинар по налоговому праву: "Принципы противодействия уклонению от уплаты налогов в Польши и России" (International scientific seminar on tax law: "The Principles of Countering Tax Evasion in Poland and Russia"), Gdańsk, 27 April 2015;
- IV International Baltic Conference on Financial Law: "The Financial Law towards Challenges of the XXI Century", Gdynia – Kopenhagen – Gdynia, 21–24 April 2017; The development and elaboration of the research program "Financial law in the face of the challenges of the 21st century";
- V International Baltic Conference on Financial Law: "The Financial Law towards Challenges of the XXI Century";
- I International Seminary of the Financial Law – Financial Law Review, Gdynia- Karlskrona-Olandia 10–13 May 2019.

In addition, three scientific conferences and two international scientific seminars related to the topic of financing local government units were organised as a result of three research projects devoted to local government finances "Local government 21":

- I International Conference on Finance and Finance Law of Local Government Units: "Sources of Local Government Financing in the Light of Modern Regulations", Gdańsk, 15–16 September 2014;
- II International Conference on the Finance of the Local Government: "Local Government Financing and its Tasks and

European Charter of Local Government. Practical Problems, Gdańsk, 25 April 2016;

- International Seminary of the Financial Law of Local Government: "Local Government Financing and its Tasks and European Charter of Local Government", Gdańsk, 25 April 2016;
- III International Conference on the Finance of the Local Government: "Local government in 20 years after the administrative reform of the country, the balance of hope and postulates for the future", Gdańsk 16 April 2018;
- International Seminar on Financial Law of Local government "Financing local government and its tasks, in the regional policy of the European Union". The conference was organised in Gdańsk on 16 April 2018.

As a result of completed research projects, the Center and the Department of Financial Law, Faculty of Law and Administration, University of Gdańsk have published over thirty volumes of publications. Their authors are hundreds of researchers from several research centres throughout Poland, the Czech Republic, Slovakia, Lithuania, Croatia, Kazakhstan and Russia. For several years, the publications have been regularly published in cooperation with the Department of Financial Law and Economics, Faculty of Law, Masaryk University in Brno and reported to the Web of Science:

- Dobaczewska, A., Juchniewicz, E., Sowiński, T. (eds.). System finansów publicznych. Prawo finansowe wobec wyzwań XXI wieku / The System of Public Finances. The Financial Law towards Challenges of the XXI Century. Warszawa: CeDeWu, 2010. (ISBN 978-83-7556-326-9 [Gdansk Uniwersity]; EAN 9788375563269. ISBN 978-83-7556-327-6 [CeDeWu]; EAN 9788375563276).
- Dobaczewska, A., Juchniewicz, E., Sowiński, T. (eds.). Daniny publiczne. Prawo finansowe wobec wyzwań XXI wieku / Public Levies. The Financial Law towards Challenges of the XXI Century. Warszawa: CeDeWu, 2010; (ISBN 978-83-7556-329-0 [Gdansk Uniwersity]; EAN 9788375563290 i ISBN 978-83-7556-328-3 [CeDeWu]; EAN 9788375563283).
- Gliniecka, J., Wróblewska, M., Juchniewicz, E., Sowiński, T. (eds.). System prawnofinansowy. Prawo finansowe wobec wyzwań XXI wieku / Law and Finance. The Financial Law towards Challenges of the

XXI Century. Warszawa: CeDeWu, 2013; (ISBN 978-83-7556-572-0 [Gdansk Uniwersity]; EAN 9788375565720. ISBN 978-83-7556-568-3 [CeDeWu]; EAN 9788375565683).

- Gliniecka, J., Wróblewska, M., Juchniewicz, E., Sowiński, T. (eds.). Prawo finansowe samorządu terytorialnego. Prawo finansowe wobec wyzwań XXI wieku / Local Finance Law. The Financial Law towards Challenges of the XXI Century. Warszawa: CeDeWu, 2013. (ISBN 978-83-7556-573-7 [Gdansk Uniwersity]; EAN 9788375565737. ISBN 978-83-7556-569-0 [CeDeWu]; EAN 9788375565690).
- Gliniecka J., Juchniewicz, E., Sowiński, T. (eds.). Finanse publiczne jednostek samorządu terytorialnego. Źródła finansowania samorządu terytorialnego we współczesnych regulacjach prawnych / Public Finance of Local Government. Sources of Local Government Financing in the Light of Modern Regulations. Warszawa: CeDeWu, 2014. (ISBN 978-83-7556-700-7 [Gdansk Uniwersity]; EAN 97883755657007. ISBN 978-83-7556-676-5 [CeDeWu]; EAN 9788375566765).
- Gliniecka, J., Drywa, A., Juchniewicz, E., Sowiński, T. (eds.). Prawo finansowe wobec wyzwań XXI wieku – The Financial Law towards Challenges of the XXI Century / Проблемы и задачи финансового права в XXI веке. Warszawa: CeDeWu, 2015. (ISBN 978-83-7556-738-0 [Gdansk Uniwersity] EAN 9788375567380. ISBN 978-83-7556-737-3 [CeDeWu]; EAN 9788375567373).
- Gliniecka, J., Drywa, A., Juchniewicz, E., Sowiński, T. (eds.). Finansowanie samorządu terytorialnego i jego zadań, a Europejska Karta Samorządu Lokalnego / Local Government Financing and European Charter of Local Self-Government. Warszawa: CeDeWu, 2016. ISBN 978-83-7556-847-9; EAN 9788375568479.
- Gliniecka, J., Drywa, A., Juchniewicz, E., Sowiński, T. (eds.). Finansowanie jednostek samorządu terytorialnego, Problemy praktyczne / Local Government Financing, Practical Problems. Warszawa: CeDeWu, 2016. ISBN 978-83-7556-843-1; EAN 9788375568431.
- Radvan, M., Gliniecka, J., Sowiński, T., Mrkývka, P. (eds.). The financial law towards challenges of the XXI century. Brno: Masaryk

University, 2017, theoretical series, edition Scientia, file no. 580. ISBN 978-80-210-8516-9.

- Gliniecka, J., Drywa, A., Juchniewicz, E., Sowiński, T. (eds.). Samorząd terytorialny w 20 lat po reformie administracyjnej państwa. Bilans nadziei i postulaty na przyszłość / Local Government in 20 years after the administrative reform. Balance of hope and postulates for future. Warszawa: CeDeWu, 2018. ISBN 978-83-8102-096-1.
- The Challenges of Local Government Financing in the Light of European Union Regional Policy, (Conference Proceedings), Petr Mrkývka, Jolanta Gliniecka, Eva Tomášková, Edward Juchniewicz, Tomasz Sowiński, Michal Radvan (eds.). ACTA UNIVERSITATIS BRUNENSIS, IURIDICA, Editio Scientia Vol. 636, Masaryk University, Brno 2018. ISBN 978-80-210-9086-6.
- Dzwonkowski, H., Gliniecka, J. (eds.). Prawo finansowe / Financial law. Warszawa: C. H. Beck, 2013. ISBN 978-83-255-5021-9.
- Gliniecka, J. (ed.). Financial Law. Gdańsk-Warszawa: Wolters Kluwer, Wydawnictwo Uniwersytetu Gdańskiego, 2016. ISBN 978-83-78-65-460-5.
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The Department of Financial Law, Faculty of Law and Administration, University of Gdańsk, together with the Gdansk University Center for Self-Government and Financial Law, have already started the fourth edition of the research project "Local Governance21" and currently work on the organisation of the 4th Local Government Finance Conference, "Challenges for local government units arising from the amendment to the acts: on public finances and maintaining cleanliness and order in municipalities".

Tomasz Sowiński

PART 1:
FINANCIAL LAW – GENERAL ISSUES

Social Clauses in Public Procurement Procedures in the Light of Public Expenditure Efficiency

Maciej Bendorf-Bundorf[1]

Abstract

The aim of this contribution is to present social clauses which can have significant influence on contract award procedure effectiveness. Description of both Polish and European regulations on chosen social clauses in public procurement is followed by assessing them from the perspective of public spending efficiency. This contribution is aimed to confirm the hypothesis that social clauses in public procurement should be considered as a method of increasing public expenditure efficiency, despite the fact that examples of the application of social clauses in practice show that their incorporation into the terms of a public contract to be awarded increases procurement costs. Used scientific methods: dogmatic, comparative, statistical.

Keywords: Public Procurement; Social Aspects; Procurement Procedure; Socially Responsible Public Procurement; Public Expenditure Efficiency.

JEL Classification: H57.

1 Introduction

Every system has to identify social values that produce economic justice and purposely designing the law to achieve fairness. (Sugin, 2018). By generating 14 % of the European Union (EU) gross domestic product, public authorities are its major procurers (Ladi, Tsarouhas, 2017: 391). Owing to their purchasing capacity, public entities can promote social inclusion, employment opportunities, accessibility and labour standards. Promotion of socially responsible public procurement strives for a greater compliance

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with social standards (Bobowski, Gola, Szydło, 2018: 89–90). The Europe 2020 Strategy [COM(2010) 2020] puts forward a priority to achieve an inclusive growth by fostering a high-employment economy which would deliver social and territorial cohesion. One of the instruments that can be used to achieve this goal is public procurement.

Most important in public procurement is the benefit determined on the basis of an economic calculation, taking into account the quality and functionality of products purchased. However, in accordance with the idea of socially responsible public procurement, contracting authorities should also take into consideration the possible social benefits which can be achieved as part of public contract award procedures (Wieloński, 2013: 132).

The aim of this contribution is to present social clauses which can have significant influence on contract award procedure effectiveness. Description of both Polish and European regulations on chosen social clauses in public procurement is followed by assessing them from the perspective of public spending efficiency. This contribution is aimed to confirm the hypothesis that social clauses in public procurement should be considered as a method of increasing public expenditure efficiency, despite the fact that examples of the application of social clauses in practice show that their incorporation into the terms of a public contract to be awarded increases procurement costs.

2 European and Polish regulations on social clauses in public procurement

European legal framework for public procurement includes: Directive 2014/24/EU of 26 February 2014 on public procurement (OJ L 094 28. 3. 2014: 65) and Directive 2014/25/EU of 26 February 2014 on procurement by entities operating in the water, energy, transport and postal services sectors (OJ L 094 28. 3. 2014: 243). Public procurement system of Poland is based on the Act of Public Procurement Law (PPL) which was adopted on 29 January 2004 (Journal of Laws of 2018, item 1986).

2.1 Social clauses in describing the subject-matter of the contract

The preparation of a contract award procedure begins with a description of the contract subject-matter. In principle, the contracting authorities are free to define the subject-matter of the contract, so that it will meet their needs. Public procurement law is not concerned with what contracting authorities purchase, but with how do they purchase it. That is why, neither of the Directives on Public procurement restricts the subject of the contracts as such (Bendorf-Bundorf, 2014: 149–150).

One of the most obvious examples of including social clauses in public procurement procedures is to describe the subject-matter of the contract so that required products, services or construction works meet specific social standards. According to the recital 76 of the preamble to Directive 2014/24/EU, for all procurement intended for use by persons, whether general public or staff of the contracting authority, it is necessary for contracting authorities to lay down technical specifications so as to take into account accessibility criteria for people with disabilities or design for all users[2]. This general principle is confirmed by article 42 of Directive.

Public Procurement Law directly refers to this matter in article 29 para. 5, which states that in the case of contracts to be used by natural persons[3] the description of the subject-matter of contract shall be drawn up with account taken of the requirements in the scope of accessibility for disabled persons or for-all design.

While describing the subject of the contract award procedure contracting authorities can also, according to article 70 of Directive, lay down special conditions relating to the performance of a contract. Those conditions may include economic, innovation-related, environmental, social or employment-related considerations.

2 According to The United Nations Convention on the Rights of Persons with Disabilities, accessibility is one of the general principles guaranteed by its article 3. Article 9 of The Convention obliges States Parties to take appropriate measures to ensure to persons with disabilities access to the physical environment, to transportation, to information and communications, including information and communications technologies and systems, and to other facilities and services open or provided to the public.

3 Including employees of the contracting authority.

The Public Procurement Law implements this regulation in article 29 para. 4. In accordance with given provision, contracting authorities may specify requirements connected with the implementation of the contract which may in particular include social or employment-related aspects, for example relating to the employment of: unemployed persons, adolescents for the purposes of professional training or disabled persons (Pieróg, 2019: 274–275).

Employment policy requirements should be defined, taking into account both Polish and EU legal regulations. Thus, when identifying the category of people to be employed to perform a public contract, it seems right to refer to the concepts of a "disadvantaged worker" or a "disabled worker" within the meaning of Commission Regulation No. 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty (OJ L 187, 26. 6. 2014: 1–78).

It needs to be emphasised that compliance with the requirement under Art. 29 para. 4 of the PPL to employ specific people may not involve the employment of certain groups of workers in general, but rather their employment to perform a given public contract. The goal of the regulation in question is to associate the employment of particular categories of people with the performance of a public contract. The requirement will not be met if such people are employed, but not used in the performance of the public contract.

According to Art. 29 para 3a of the PPL, in the description of the subject-matter of contract for services or works, the contracting authority shall define the requirements relating to the employment by an economic operator under an employment contract of persons carrying out activities indicated by the contracting authority in the scope of implementation of the contract (Zalewska, 2018: 18), if the said activities are to be carried out in the manner defined in Article 22 § 1 of the Act of 26 June 1974 – Labour Code (Journal of Laws of 2018, item 917).

The obligation to introduce the requirement to employ workers under an employment contract into the terms of a public contract to be awarded is a sign of the legislature's will to ensure compliance with the labour law while performing public contracts and to disallow the practice of concluding

contracts under civil law whenever it is unjustified by the nature of a relationship. Allowing the said practice, i.e. acknowledging the non-employee status of a worker, means that the worker's legal status while performing work is less favourable (e.g. due to the lack of right to vacation, the lack of salary protection, existing liability for damages, the lack of a right to protective clothing, etc.), while the employer bears lower costs, earning the same benefits as from the work of a worker employed under an employment contract (Opinion of the PPO on the subject of Art. 29 para. 3a of the PPL, taking into account the common position of the President of the Public Procurement Office and the Inspector General for Personal Data of 28 April 2017).

2.2 Social clauses – reserved contracts

The most restrictive and controversial social clause is set forth in Art. 20 of Directive 2014/24/EU. The provision empowers Member States to reserve the right to participate in public procurement procedures to sheltered workshops and economic operators whose main aim is the social and professional integration of disabled or disadvantaged persons or may provide for such contracts to be performed in the context of sheltered employment programmes, provided that at least 30 % of the employees of those workshops, economic operators or programmes are disabled or disadvantaged workers.

According to the recital 36 of the preamble to Directive 2014/24/EU, employment and occupation contribute to integration in society and are key elements in guaranteeing equal opportunities for all. In this context, sheltered workshops can play a significant role. The same is true for other social businesses whose main aim is to support the social and professional integration or reintegration of disabled and disadvantaged persons, such as the unemployed, members of disadvantaged minorities or otherwise socially marginalised groups. However, such workshops or businesses might not be able to obtain contracts under normal conditions of competition. Consequently, it is appropriate to provide that Member States should be able to reserve the right to participate in award procedures for public contracts or for certain lots thereof to such workshops or businesses or reserve

performance of contracts to the context of sheltered employment programmes (Sołtysińska, Talago-Sławoj, 2016: 275).

The Polish legislators have implemented the provision of Art. 20 of Directive in Art. 22 para. 2 of the PPL, which states that the contracting authority may stipulate in the contract notice that only sheltered workshops and other economic operators may compete for a contract whose activities, or activities of their separated organisational units which will perform the contract, includes social and professional integration of persons belonging to socially marginalised groups, in particular: disabled persons, unemployed persons, persons deprived of liberty or released from prisons, persons with mental disorders, homeless persons, persons granted by the Republic of Poland a refugee status, persons up to 30 years of age and persons who have reached 50 years of age with a job-seeker status and unemployed, persons belonging to disadvantaged minorities[4] (Granecki, 2016: 290–291).

The principal objective behind the introduction of the regulation in question was to improve access to the public procurement market for contractors employing people with disabilities, thus striving for a higher level of integration or re-integration of people with disabilities in the labour market (Justification for the bill amending the Public Procurement Law Act and the Act on Court Fees in Civil Cases, Note 2154). A similar provision is determined in Art. 138p of the PPL.

However, a question might be raised about the legitimacy of introducing Art. 22 para. 2 of the PPL when one takes into account the basic principles of public contract award procedure, particularly the principles of equal treatment and fair competition. They are of utmost importance under the Public Procurement Law and are of particular significance regarding the implementation of the basic aims of the Act, i.e. ensuring that public funds are spent efficiently as well as that all operators guaranteeing good performance have access to public procurement (Stachowiak, Jerzykowski, Dzierżanowski, 2010: 105). From the standpoint of operators that do not meet the said

4 Art. 22 para. 2a specifies that the contracting authority shall define a minimum percentage level of employment of the persons belonging to one or more categories referred to in para. 2 not lower than 30 %, of persons employed by sheltered workshops or economic operators or their units referred to in para. 2.

employment requirement, the application of Art. 22 para. 2 of the PPL completely prevents access to a given public contract award procedure. It needs to be added that such an extensive restriction of competition may also entail adverse consequences for the contracting authority. Narrowing down the group of potential contractors as part of a given public contract award procedure may lead to no bids submitted to the contracting authority, which will then be forced to carry out the entire procedure again.

In contract notices published in the Public Procurement Bulletin in 2017, contracting authorities placed such a stipulation in 294 cases, which accounted for 0,24 % of the total number of procurement procedures. In 2016 there were 223 (0,21 %) procedures with this stipulation, in 2015 – 169 (0,15 %), and in 2014 – 183 (0,13 %). Most of them were public service contracts – 164 notices, followed by public supply contracts – 69 notices and public works contracts – 61 notices (Report of the President of the Public Procurement Office on the functioning of the public procurement system in 2017: 49).

2.3 Social clauses as a premise of exclusion of economic operators

Social clauses are also found in the provisions regulating the conditions of exclusion from contract award procedure. Prohibiting certain economic operators form obtaining government contracts is essential from the point of view of including social considerations in public procurement procedure. Excluded are those bidders who are guilty of previous wrongdoing and violated particular standards of social behavior (Buying social: A guide to taking account of social considerations in public procurement: 20).

The eligibility criteria for economic operators are set out in Art. 57 of Directive 2014/24/EU. They are aimed at establishing the trustworthiness of a potential business partner. These criteria, which may give rise to the exclusion of a bidder or a candidate from the procedure, primarily concern their proper operation in the market under the applicable laws and regulations. Art. 57 para. 2 states that an economic operator shall be excluded from participation in a procurement procedure where the contracting authority is aware that the economic operator is in breach of its obligations

relating to the payment of taxes or social security contributions and where this has been established by a judicial or administrative decision having final and binding effect in accordance with the legal provisions of the country in which it is established or with those of the Member State of the contracting authority (Skubiszak-Kalinowska, Wiktorowska, 2017: 332).

In the Polish legal system, reasons for excluding an economic operator from a public contract award procedure are governed by Art. 24 of the PPL. In particular, excluded from contract award procedure shall be an economic operator for whom a final verdict or final administrative decisions has been issued on arrears in payment of taxes, levies, or social or health insurance premiums. Furthermore, the contracting authority may exclude an economic operator:

- with regard to which a final administrative decision was issued on the infringement of obligations resulting from the provisions of labour law, environment protection law, or social security provisions[5],
- that infringed the obligations relating to the payment of taxes, levies, or social or health insurance premiums, which the contracting authority is able to demonstrate with the use of relevant evidence[6].

3 The influence on the public spending efficiency

3.1 Social description of the subject-matter of the contract

The freedom to define the subject of a public contract to be awarded, including requirements of a pro-social nature, is limited by the duty to respect the principles of fair competition and equal treatment of all economic operators (Zdebel-Zygmunt, Rokicki, 2014: 53). Requirements regarding social standards must not constitute a measure that directly or indirectly renders it difficult for foreign contractors to access a domestic public procurement market. First and foremost, this means that social standards (compliance with which is requested) need to be associated with the subject of the public

5 If by this administrative decision a fine was assessed in an amount not lower than PLN 3000.

6 Unless the economic operator has paid due taxes, levies, and social or health insurance premiums with due interest or penalties, or entered into a binding agreement on the repayment of these liabilities.

contract. In addition, the acceptability of introducing such requirements into the terms of a public contract to be awarded hinges upon formulating them in a non-discriminatory manner, allowing compliance with such requirements by all economic operators, regardless of their country of origin or residence (Buying social: A guide to taking account of social considerations in public procurement: 23–24).

To ensure that contractors from all over the European Union have the widest possible access to domestic markets is the core function of public procurement in the pan-European perspective. Any restrictive measures in this respect may entail a drop in public spending efficiency. The isolation of domestic markets and exclusion of competitors being foreign operators may translate into bids with prices higher than those offered when there are other operators to compete with, also from other EU Member States.

Evaluation of public spending efficiency may prove problematic when it comes to Art. 29 para. 3a of the PPL. What can directly increase prices in bids submitted is the contractor's obligation (referred to in said article) to incorporate into the terms of a public contract to be awarded the requirement for a contractor and subcontractors to employ, under a contract of employment, people executing tasks specified by the contracting authority as part of the performance of the public contract. The contractor and subcontractors obligated to enter into contracts of employment with specific workers are to bear higher costs of providing services or carrying out construction works. As a consequence, the contractor will accordingly increase the price of its bid, which is justified from the point of view of economic profitability of a given public contract. How then to assess such cases from the standpoint of public procurement efficiency? Does an increase in the price of a specific service or construction work financed with public funds mean that public spending is less efficient?

3.2 Reserved contracts

Reserved contracts, regulation under Art. 22 para. 2 of the PPL, may cause similar doubts. In express terms, the provision equips the contracting authority with the possibility to restrict access to a given public contract, exclusively allowing a specific group of economic operators to submit their bids. Thus,

there are decreasing competition factors in a procedure, which may directly translate into higher prices offered. Therefore, similarly to Art. 29 para. 3a of the PPL, evaluating the financial efficiency of public contract award procedure, one ought to assume that social clauses have a negative impact on the aspect in question.

Modern public contracts, containing social clauses, are intended to serve not only functions of purchasing goods and services for the public sector but also specific social functions (Corvaglia, 2016: 611). A given public expense may satisfy the demand of a contracting authority for a specific supply, service or work and may serve the purposes of employment policy or social integration of individual categories of people (Murphy, Eadie, 2019: 138; Barnard, 2017: 211–212). Due to the multiplicity of functions, one needs to accept that social public contracts have increased efficiency when compared to purchases which do not require the application of social clauses.

3.3 Exclusion from contract award procedure

Of a less problematic nature as far as the efficiency of the public procurement system is concerned, seems to be social clauses present among the grounds for exclusion of economic operators from a public contract award procedure. One has to recall that the grounds referred to in Art. 24 of the PPL are to verify the 'personal' status of contractors that seek to perform a public contract. Exclusion of certain operators from public procurement is intended to ensure that a given public contract will be awarded only to a contractor capable of providing a good performance bond. One may speak of an efficient public spending system only in the case of performance of a public contract in a timely manner and in compliance with the terms of the said contract. The grounds of a pro-social nature referred to in Art. 24 should also be considered factors allowing for the verification of operators wishing to perform a public contract as well as for the evaluation of their reliability in social and economic terms. Therefore, it is reasonable to conclude that social clauses set out in Art. 24 of the PPL directly increase the efficiency of public procurement.

4 Conclusion

Social aspects can be considered at various stages of contract award procedures. Form the point of view of the topic of this contribution the most significant is the phase of describing the subject-matter of the contract, as well as the phase of defining the conditions for participation in the procedure to be met by economic operators and establishing the terms of exclusion. We need to emphasize that according to the general principle of public procurement procedures, the contracting authority shall prepare and conduct contract award procedures in a manner ensuring fair competition and equal treatment of economic operators.

Public procurement represents an important part of the market in the economic sense (Gola, 2018: 105). The main purpose of an efficiently functioning public procurement system is to obtain as much as possible from the expenditure incurred. This should be understood as efficient achievement of the public contract's purpose to the greatest extent, whose purpose is to satisfy a specific need of the contracting authority. However, an increase in costs of a single public contract being the result of the application of social clauses should not constitute grounds for claiming that the public procurement system efficiency has decreased. The efficiency of public spending needs to be considered in a context broader than savings of an individual contracting authority and the costs of a specific public contract. Modern public contracts, containing social clauses, are intended to serve not only functions of purchasing goods and services for the public sector but also specific social functions. A given public expense may satisfy the demand of a contracting authority for a specific supply, service or construction work and may serve the purposes of employment policy or social integration of individual categories of people. Due to the multiplicity of functions, one needs to accept that socially responsible public procurement has increased efficiency when compared to a purchase which do not require the application of social clauses.

Examples of the application of social clauses in practice show that their incorporation into the terms of a public contract to be awarded increases procurement costs. However, it appears that when one considers this issue

in the long term, it might turn out that when it comes to public spending, social clauses help save money (Interview with Komorowski, 2012: 18). After all, one of the goals of social clauses in public procurement procedures is to increase the employment of the disabled or the unemployed, which as per the core principle of public spending efficiency may prove financially beneficial, e.g. in the form of lower budgetary spending on social aid (Koba, 2010: 6–7).

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Responsibility for Non-Recovery of Civil Law Claims of the State Treasury and Local Government

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Abstract

The article presents the problems of recovering unpaid receivables of the State Treasury and local government. It has been demonstrated that it is justified to privilege the State Treasury and local government in the scope of simplifying the procedure of claiming due debts, as losses in this respect may pose a threat to the stability of public finance and the possibility of implementation of public tasks.

A person, guilty of allowing the State's debt claim to be time-barred, should only pay a financial penalty which would be a total compensation for lost of profits in the case of small amounts, and in the case of large amounts – a partial compensation. It has also been proved that the State Treasury and local government should be privileged in establishing collaterals for receivables.

Keywords: The State Treasury; Local Government; Receivables; Obligation.

JEL Classification: K49, K39, K10

1 Introduction

Public revenues are divided into public levies and property income, i.e. income from lease contracts, rental contracts and other agreements of similar nature, dividends from shares in capital companies, interest, inheritance, bequests and donations in cash, income from the sale of assets, things and rights, revenues from sale of goods and services provided by units of the

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public finance sector entities and other income due to public finance sector entities resulting from acts or international agreements (Glumińska, 2010: 857). The State Treasury and local government may conclude civil law agreements, for example lease or rental contracts, aimed at making public property available for a fee for temporary use, contracts for the sale of property, services, exchange agreement with subsidy for the State Treasury or local government, or interest-bearing loans (Act on public finance law, Art. 6, Art. 115, Art. 224). Radvan stressed that municipalities are creditors for their own properties, which is used by somebody else against payment or they stand as tax administrator and collect local taxes (Radvan, 2017: 340–348) or administration fees. In the case of conclusion of these contracts there exist public revenues. Not always parties, who conclude agreements with the State Treasury or local government, meet the obligation to pay debts timely, for example to pay the rent, sale price, interest on the loan or they do not want to perform obligations towards the State Treasury or local government. In the event that an entity fails to pay civil claims, as a result of the negligence in their investigation, they will be time-barred, and some public revenues will be lost. This is at the expense of all those (Zalcewicz, 2017: 247) who regularly pay public levies (citizens, entities conducting business activity) and entities which, due to their situation, are rewarded by public sector entities, i.e. those receiving subsidies, social assistance benefits (grant-in-aid), pensions. Justice requires that if an entity, that has not performed a monetary liability to the Treasury or local government, was effectively forced to do so. Persons who are responsible for the recovery of unpaid debts to the State Treasury and local government, and whose negligence in their duties led to the limitation of monetary obligations under civil law congracts, due to the State Treasury or local government, should bear consequences.

The purpose of the article is to examine:

- whether in the scope of pursuing civil law liabilities due to the State Treasury and local government, the aforementioned entities should be privileged,
- what responsibility should be borne by persons who led to losses in public revenues as a result of limitation of claims due to the State

Treasury and local government, and indication of legal solutions regarding effective recovery of civil law liabilities of the State Treasury and local government.

The study used a dogmatic method to analyze the applicable legal provisions, a functional method in the scope of how the proposed solutions will affect practical activities and the study of literature related to the topic.

2 Premises for effective debt recovery

Failure to pay on time due debts of the State Treasury and local government is a threat to the timely implementation of public tasks by these entities. Even if those are small amounts due to rent or lease, they can not be underestimated, in particular if there are many unpaid amounts from civil law contracts on time. Persons responsible for the recovery of claims under civil law contracts should be obliged to take immediate action to recover unpaid debts on time. The universality of making payments using bank transfers means that the beneficiary of the transfer receives the payment not later than on the second business day from the transfer. Persons responsible for recovery of claims of the Treasury and local government, in the event of failure to pay the obligation on time, on the fourth day should send to the debtor, according to agreed instructions, a payment request and inform that failure to pay within 14 days from sending information will initiate proceedings aiming at compulsory payment of the due amount. While contacting the debtor, the forms of electronic communication should be legitimized equally to the letter sent using the postal operator. The request for payment sent via SMS, e-mail, messenger or other means of communication, that will arise in the future, should be equivalent to sending a letter through the postal operator. The means of electronic communication have the advantage over a traditional postal operator as they are much faster and cheaper. Taking further actions aimed at compulsory recovery of receivables should not depend on the debtor's confirmation of receiving a request for payment. A debtor who is in default should bear the risk of receiving information on the amount due.

A compulsory proceeding regarding the recovery of claims due to the State Treasury and local government may be carried out by a court or without

the participation of a court. The argument for the first solution is the equality of entities, including the State Treasury and local government, under the law. Judicial way of recovering debts may cause delays in the recovery of claims (Sonnemans, 2011: 689), due to workload of the courts. Court proceedings allow to eliminate possible errors of persons responsible for pursuing the claims of the Treasury or local government, in particular when the case was launched illegitimately, for example when the party paid all the receivables on time and the payment was not noticed by the public entity, for which the payment was made, due to incorrect registering. Claiming due debts without the participation of the court allows to eliminate one stage in the recovery of due debts what speeds up the entire proceedings. However, in such cases, it is not possible to exclude the abuse of right to issue enforcement titles allowing the execution without the involvement of the court. Such cases occurred, for example, in Poland when banks could issue bank enforcement titles to debtors on the basis of bank documents. Due to abuse of this privilege, i.e. carrying out the execution of unmatured liabilities, banks were deprived of issuing bank enforcement titles and later also bank executory titles which allowed for execution by giving the enforcement clause in court in a short, three-day, period. The term was instructional in nature and in practice it did not happen that it was adhered to by the courts. Usually courts issued enforcement clauses within a few months.

In a democratic state the recovery of claims, including the State Treasury and local government, should take place with the participation of the court whose task is to check whether the demandable debt exists and to issue an executory clause allowing for proper enforcement proceedings. Proceedings before a court to give the enforcement clause should be simplified and quick. A public entity claiming due debts should be able to submit to the court an application for appending the enforcement clause in an electronic form, together with the necessary attachments in the same form. The court should consider a case, represented by one judge, within 14 days from the moment of receiving a complete application. A debtor and a creditor should be informed about the hearing by means of various forms of communication (choice of court), including electronic (mail, SMS), while the hearing could also take place without the participation of the parties.

A court ruling on the appending of the enforcement clause would be legally valid and would not be subject to appeal in the same way as a decision dismissing the application for granting the enforcement clause. The fourteen-day period for the court to issue a ruling on the granting of an enforcement clause should be of a mandatory and non-negotiable nature.

Granting an enforcement clause to the writ of execution by the court, enabling bailiffs to carry out executory proceedings, does not mean that the State Treasury, or local government, will quickly recover the amounts due. The enforcement authorities should be obliged under law to prioritize and carry out the enforcement of claims of the State Treasury and local government, before other cases. The proceedings dismissed by the enforcement authority, eg. due to the lack of assets from which enforcement can be carried out, should be resumed at the request of a public entity indicating the existence of debtor's assets from which execution can be carried out without the need to re-issue the enforcement clause by the court.

In the case of bankruptcy of the State Treasury or local government's debtor, the civil law liabilities of the Treasury should be satisfied first of all from the bankruptcy estate equally to employees' liabilities due to arrears, unpaid taxes, customs duties and public and legal fees.

The limitation periods for civil law liabilities of the State Treasury, local government, should be extended in relation to the limitation of claims of other entities. Persons involved in the registration of payments from civil law contracts to the Treasury may, by inaccuracy or due to workload, not notice that some entity is in arrears in payment. The confirmation of the occurrence of due receivables may take place as a result of the control. Conducting frequent controls is costly for public finances, as it usually requires the employment of additional, well-qualified and experienced people. The extension of the limitation period for civil law claims of the State Treasury, local government, partially solves the problem of not establishing the immediate existence of due debts. The limitation period for civil law liabilities of the State Treasury and local government should be at least 10 years.

The aforementioned solutions would privilege the State Treasury and local government in the scope of pursuing their payable claims under civil

law contracts in terms of the speed of the entire proceedings, facilitating the information of the debtor about the court hearing and prioritising the proceedings by the enforcement authorities. However, it is justified due to the stability and certainty of public revenues that are necessary for the State Treasury and local government to perform their functions.

3 Consequences for the employees responsible for non-investigation of civil law claims

The best legal regulations facilitating the recovery of due and payable receivables of the Treasury or local government will be insufficient, if the employees responsible for recording the receivables due, sending requests for payment or preparing and submitting an enforcement proceeding application to the court will disregard their duties, prove irresponsible employees and will cause civil law claims to be time-barred. The employee's failure to fulfill obligations related to non-investigation of civil law liabilities should be punishable. In Poland, non-investigation of due claims of the State Treasury and local government is considered to be a violation of public finance discipline (Act on responsibility for violation of public finance discipline, Art. 5). Pursuant to this provision it is punishable not to recover receivables from rent for flat or commercial premises belonging to the local government, fees for advance payments to cover the costs of managing the common real estate, repair fund and other charges for the supply of utilities, refuse disposal, sewage disposal, for undue bonuses on the price of real estate included in the housing register, district receivables due to the sale of residential premises to their tenants, contractual penalties, interest for delay in payment, lease contracts or fines imposed for the purpose of compulsion (Lipiec-Warzecha, 2010: 86) (Bolek, 2012: 45).

The following penalties may be imposed on the employee guilty of non-investigation of civil law claims of the Treasury and local government (Act on responsibility for violation of public finance discipline, Art. 32): admonition, reprimand, penalty payment ranging from 0,25 to 3-times the monthly remuneration of the person responsible for violation of public finances discipline or a ban on performing functions related to the disposal of public funds for a period of one to five years. When judging a penalty for not

recovering the State Treasury or local government's s claims, the authority (the adjudicating committee) imposes a penalty at its discretion (Dębowska-Sołtyk, 2015: 45), taking into account the level of public finance harmfulness, degree of guilt, social punishment goals, preventive and disciplinary goals to be achieved in relation to the punished person, taking into account the relationship between the amount of the financial effect and the amount of expenses or costs specified in the financial plan of the public finance sector entity (Act on responsibility for violation of public finance discipline, Art. 33). The penalty of prohibition of performing functions related to the disposal of public funds is imposed in the case of gross violation of public finance discipline and in the case of repeated punishment for violation of public finance discipline (Act on Responsibility for violation of public finance discipline, Art. 33). A fine or a reprimand is imposed in the event of violation of public finance discipline, the level of which is harmful for public finances (Sekuła, 2018: 13), however a fine is imposed, if, due to the violation, the State Treasury or local government claim was not paid in large amount (Act he responsibility for violation of public finance discipline, Art. 34a). There is no responsibility for failure to recover the claims of the Treasury or local government, when the level of harm (Borowska, 2015: 23) to public finances is negligible (Act on responsibility for violation of public finance discipline, Art. 28).

Penalties that may be imposed on a person guilty of failure to recover the State Treasury's receivables may be inadequate to losses (Gontarczyk-Skowrońska, 2013: 35) suffered by the State Treasury or local government as a result of non-payment of due debts. There may arise situations when taking actions aimed at recovering due debts, sending a letter requesting payment of due liabilities by means of a postal operator, has a greater value than the amount of the claim. It happens, for example, in the case of payable annual perpetual usufruct fees for land, valued less than EUR 1, while the costs of sending a request for payment amount to over EUR 1. In such cases non-recovery of due receivables due should not be punished, unless the law allows to send a request for payment of outstanding debts in a cost-free manner using electronic means of communication, eg. by e-mail.

However, if there are many such cases, then the recovery of due debts is a must, as numerous minor unpaid debts arise to considerable amount.

Penalties that may be imposed on a person guilty of non-investigation of claims of the Treasury, or local government, in accordance with Act on responsibility for violation of public finance discipline, does not have to be necessarily financial, which is not a good solution. If an obligatory financial penalty for failing to recover time-barred claims would be imposed on persons guilty of these omissions in the amount equal to the overdue debt with interest, there would be no loss for public finances. In the case when the amount of time-barred claims exceeds multiplicity of the remuneration of the person guilty of such fail, the fine could not be higher than multiplicity of the average remuneration of public sector employees. When liabilities due to the State Treasury and local government are not time-barred, less retributive penalties should be imposed on persons failing to recover such liabilities, eg. an admonition or a reprimand, and if the amount due was small, i.e. less than EUR 50, the person should not be fined but only incur the costs of proceedings regarding the violation of public finance discipline. The penalty of banning from performing functions related to the disposal of public means for a period of one to five years is most painful for employees in charge of managerial positions and for employees awaiting promotion. However, it does not provide any compensation for depleted public finances as a result of failure to recover due debts. It is not advisable to impose this penalty for failing to recover due liabilities of the Treasury or local government.

4 Preventive facilitation of recovering due debts

The payment of claims, including future claims, may be secured. The debtor may establish the following security for the repayment of the claim: deposit (Niezbecka, 2000: 410), power of attorney to dispose of the bank account (Troicka-Sosińska, 1997: 56), blockade of funds on the bank account (Krzemińska, 1998: 315), an ordinary pledge on movable property (Mojak, 2004: 9), mortgage on immovable property (Rudnicki, 2003: 44) or in blanco promissory note (Heropolitańska, 2004: 72). The easiest and fastest way for the creditor to recover the amount of the unpaid debt is the case of establishing a deposit and blocking funds on the bank account when

their amount is higher than the due claim. A secure solution for debt repayment is a pledge on debtor's movable property and mortgage on immovable property because their disposal does not result in the loss of execution from the subject of security, regardless of who owns the property, however it requires enforcement proceeding by the court and by the enforcement authority (bailiff). Nevertheless, there are rare cases where the debtor may establish a bail or a block of the funds on the bank account, of which he is the holder, in the amount equal to all liabilities in a multi-annual period resulting from a contract concluded with the State Treasury or local government. Issuing a blank promissory note may be ineffective when debtors do not have any assets at the time when the enforcement proceeding is initiated against them.

Non-debtors may provide collateral not for their claims by concluding a contract with an unconditional guarantee, a surety under civil or exchange law or by encumbering their property with a mortgage or pledge. The safest way for a creditor to secure the repayment of a claim by a third party is an unconditional guarantee issued by an entity with a stable financial situation, eg. a bank, and a pledge or a mortgage on the assets of third parties. An unconditional warranty allows for the recovery of claims without the need to conduct enforcement proceedings. The burden of such proceedings may be borne by the guarantor when the payment from the sum of guarantee takes place. Under civil and exchange law, sureties granted by a third party have a limited significance because at the time of execution, the entity, who established the collateral, may not have any assets from which it will be possible to effectively enforce due debts of the Treasury and local government.

It is possible to consider whether the entity that concludes a contract with the State Treasury, or local government, on the basis of which it will pay, should provide security for the repayment of future debts. However, it is not possible to force the Treasury, or local government, to make sure that each time an agreement is concluded, on the basis of which payments were made to their benefit, debtors set up a collateral. In particular, this would apply to low-value contracts. Establishing a collateral is legitimate when the amount of debt to pay from the contract is substantial.

It would be more advisable to adopt a solution by which if any outstanding amounts due to the State Treasury or local government arise from concluded contracts, it would be possible to establish a judicial mortgage on real estate and a pledge on movable property and rights, such as securities, without the court's participation, and by merely making a statement by the creditor about the existence of due debts. This solution would secure the interests of the State Treasury or local government against the loss of due liabilities, if the creditors had a property that the creditor would know of. For this purpose, before concluding the contract, third parties would disclose their movable and immovable property under the threat of criminal liability for providing false or incomplete information. This solution would not ensure that, in the absence of a voluntary repayment, it would always be possible to execute the debtor's assets, because after concluding contract the debtor may dispose the property or encumber it for the benefit of other entities that will be entitled to the amount first claimed. This proposal increases the chances of regaining the receivables of the Treasury and local government.

5 Conclusion

An entity that successfully avoided payment of the State Treasury and local government claims, as a result of failure to recover them, obtains a type of public aid that does not require any registering. It happens at the expense of all entities that pay back the receivables to the public sector. This situation means a loss for public finances. We should create not only legal regulations that will punish those responsible for not recovering the State Treasury or local government's claims, but also regulations that will facilitate the recovery of due debts. Punishing a person guilty of not recovering due claims does not mean that the loss is completely eliminated, in particular when the amount is high.

The proposed legal solutions concerning privileging the public finance sector units in the scope of facilitations in conducting enforcement proceedings, creating simplifications and accelerations of such proceedings, would increase the certainty of income of these units. This would also apply to facilitating the establishment of compulsory securities on the debtor's assets.

The system of penalties for non-recovery of receivables of the State Treasury, or local government, should have secondary significance in terms of seeking to recover unpaid amounts from civil law contracts. Responsibility for failing to recover the overdue receivables should only consist of imposing a financial penalty on a person guilty of losses up to a maximum equal to multiplicity of the average remuneration. In the event that it is still possible to claim due receivables of the Treasury, or local government, employees guilty of negligence in this respect should be punished less and in more adequate way, for example by giving a warning.

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Non-clinical Critera in the Procedure of Assessing the Public Funded Health Care Policy Programs – Systematic and Financial Aspects

Szymon Moś[1]

Abstract

The article, starting with the constitutional roots of non-clinical criteria of health technology assessment in Polish legal system, has on purpose to prove that the legal instruments used by the legislator to introduce the non-clinical criteria to the health care policy programs assessment procedure partially lead to contradictions and ambiguity caused by interfering with the financial independence legally granted to the organizers of the programs. The article claims that this results from the direct application of the non-clinical criteria applied in the procedure of qualifying the health care services as guaranteed in the health care policy programs assessment process.

Keywords: Public Funded Health Care; HTA; Health Care Policy Programs; Non-Clinical Criteria.

JEL Classification: K32; I18; H51; H75.

1 Introduction

Health care policy programs provide organized frames for acting in favour of protecting public health, defined as an social effort for preventing, promoting and restoring human health (Pietraszewska-Macheta, 2018: 435)[2].

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2 According to the Article 5.29a of the Act on Public Funding of Health Care Services, the legal definition of the health care policy program is as follows: 'A set of planned and intended actions from the scope of health care, developed, implemented, carried out and financed by the minister or the local government unit, assessed as effective, safe and reasoned, enabling the projected aims – consisting in detecting and realizing specific health needs and improving the state of health of the specified group of beneficiaries – to be achieved within specified time limits'.

Under the Act on Public Funding of Health Care Services, ministers or local government units are the organizers of the programs. This includes development, implementation, realization and funding. The programs are assessed with regard to clinical and non-clinical criteria set for the procedure of qualifying the health care services as guaranteed.

The criteria roots may be inferred from the constitutional rules on health care. Thus, laying down provisions that take the non-clinical criteria into the consideration in the assessment of the health care policy programs is fully justified and legitimate.

2 Non-clinical assessment criteria in Polish legal system

2.1 Constitutional basis for the non-clinical criteria in general

Article 68 of the Constitution demands public authorities to establish through act the conditions and scope of the publicly funded health care services, ensured too all citizens – providing equal access irrespective of their material situation. The provisions of the Article 68 were a subject of clarification by judiciary. *Inter alia,* it was examined if there is any limitation of public health care funding allowed, regarding the broadly sensed economical (financial) or similar factors, due to limited amount of funds. The rulings opened up door for introducing non-clinical factors.

Firstly, The Constitutional Tribunal in the reasons for its Judgement dated 7 January 2004 – based exactly on to this very Article 68 – clarified that the health care system provided by public authorities cannot create illusive rights for the beneficiaries. Thus, the system has to be effective (The Constitutional Tribunal: K 14/03).

Then, the Supreme Court expanded on the issue. In the Judgment dated 9 June 2005 the Supreme Court underlined in the reasons: "*Shortage of funds for the healthcare in general as a result of several reasons (demographic, economic, organizational, moral) requires either limitation of health care services available in medical science and practice or choosing the most effective ones*" (The Supreme Court: III CK 626/04)[3].

3 Both invoked rulings focus around now outdated rules, nevertheless the remarks on the Constitutional matter are relevant and up-to-date.

Therefore, the rulings allowed non-clinical[4] criteria to be included into the process of deciding whether health care services should be funded with public funds. These criteria tend to fulfil a function of some sort of a public-payer-dedicated-tool to control public expenditures (Stewart et al., 2010: 2120). The process itself could be in other words named a health technology assessment (HTA).

2.2 Legal introduction of the non-clinical criteria to the system

Non-clinical criteria[5] were introduced in the Polish legislation in the act establishing the guaranteed health care services package[6]. The set of criteria of qualifying the health service as guaranteed was given as the basis for responsible decision-making minister[7] to decide in the services qualification process[8]. By adopting the act, Polish legislator intended to render general health insurance system more transparent and precise (*Bill 1590*: 26–37).

Introducing non-clinical criteria was also an outcome of growing influence of the broadly sensed effectiveness factor and growing importance of its measurement in the health care systems. This was followed by the desire of the public authorities to responsibly manage and rationally spend public funds: limiting the negative consequences of less competitive and public-payer-dominated health care markets became key tasks in the field of the state's regulatory role (Jacobs et al., 2013: 18–19).

Already upon the adoption of the package, the forecasts assumed increased burden on the public finances in general, coming from publicly funded health care services. Since dealing with this kind of issue requires taking actions providing boost of spending effectiveness to contain increasing

4 Alternately: "non-medical".
5 Along with the clinical ones.
6 Further referred to as "the Package".
7 The criteria should not be mistaken for any sort of obligation to enter a fulfiling service on the guaranteed package.
8 The package itself from the legal point of view was a milestone in the field of the public funded health care system in Poland. Practical issues are a matter for seperate discourse – especially the scope of guaranteed services is debatable.

expenditures (Ciżkowicz, 2011: 74–76), these reasons also guided the legislator, as it was reflected in the explanatory memorandum to the draft (*Bill 1590:* 38–41).

3 Health technology assessment and non-clinical criteria in introducing health care policy programs

3.1 Non-clinical criteria in the procedure of qualifying health care services as guaranteed

As it was stated, the criteria of qualifying the health care services as guaranteed should be referred to when considering the assessment of the health care policy programs. It is so due to applying those criteria, in the procedure of assessment of the programs.

Two non-clinical criteria of HTA may be distinguished in the Act On Public Funding of Health Care Services. They both are introduced in a descriptive way, by mentioning two categories[9] and both of them could be assigned to effectiveness and financial-worthiness (*Bill 1590*: 28).

The first one is described as a ratio between costs and achieved health results. The second is by description a financial implication to the health care system, including the financial implications to entities obliged to publicly fund the health care services.

Constructed on the effectiveness and financial factor, the taken criteria are an example of the efforts directed at improving the ratio between costs and benefits (results) on every field of the health care system. They seem to be an attempt to balance out expectations – often contradictory – of beneficiaries (interested in getting as many services as fast as possible, free of charge), healthcare providers (seeking to gain as much profits as possible and to get work satisfaction) and broadly defined public authorities (aimed at fulfilling aforesaid demands, maintaining sealed and stable funded system) – in circumstances where resources ale limited. With the criteria, the legislator also seems to recognize and share the attitude that mere

9 Public Funding of Health Care Services Act, Article 31a paragraph 1 point 6 and point 7 respectively.

increased health care funding would not have the desired positive results (Krasucki, 2005: 106–107, 118–119).

3.2 Agency for Health Technology Assessment and Tariff System

The powers of health technology assessment (HTA) are vested in the Agency for Health Technology Assessment and Tariff System[10] (also further referred to as: the Agency or AOTMiT).

AOTMiT was introduced in parallel with the package and designed as an independent HTA agency, an expert guard on conducting the proper HTA analysis[11] (Ziobro et al., 2012: 163–164). It also covers related fields with public funding of health care services as a common denominator. Thus, by its President[12], the Agency also plays an important role in the process of adopting and introducing health care policy programs. This role shall be described separately further below.

AOTMiT is a separate, central authority, with clear defined competences and agenda. AOTMiT is a state legal person[13] in terms of the Public Finance Act. The President of the Agency is its only acting body[14], so that the power and responsibility are concentrated – which allows the President to pursue adopted agenda and transparently represent Agency's position on the issues (Baka et al., 2010: 273).

There is also Transparency Council by the President as an opinion-giving and advisory body. Composed of experts with proper knowledge for conducting

10 Polish name: "Agencja Oceny Technologii Medycznej i Taryfikacji"

11 The Agency briefly describes itself: "*The role of AOTMiT is to assess and appraise all medical technologies and services claiming public money founding. […] Core activities of AOTMiT is also connected with producing health technology assessment (HTA) reports […]*" (Agencja Oceny Technologii Medycznych i Taryfikacji, n.d.).

12 Polish title: "Prezes".

13 State legal person is established by a seperate act to fulfil public tasks. Financial plans of legal persons in the past had becom regulary attached to the each Budget Act and finally became a part of the public finance sector codified in the Public Finance Act. (Smoleń, 2012: 180–181; Misiąg, 2015: 50).

14 The minister with the responsibility for health, on the recommendation of the President, appoints a deputy.

HTA, it has its own significant competences[15]: issuing opinions and taking positions alongside or at least legally required before the President's own opinion.

Some remarks on the non-medical criteria can be also made in connection with the composition of Transparency Council, since among 20 members of the council: 4 are appointed by the minister with responsibility for health, 2 by the President of the National Health Fund and 2 by the President of the Office for Registration of Medicinal Products, Medical Devices and Biocidal Products.

Thus, 40 % of the council are designated directly by the offices relevant to health care system in terms of its funding and organisation. *Prima facie* it may give an impression of strengthening the non-clinical aspects of HTA made by the AOTMiT. On the other hand, only 10 % of the council members are appointed by the most essential player in the field of public funding – the National Health Fund[16].

Therefore, strengthening the Agency's non-clinical assessment competences is not secured with the systemic solution and depends on personal matters of the composition of the council.

3.3 The AOTMiT President's assessment of the health care policy programs regarding the non-clinical reference standards

To proceed by the organizer with funding the newly prepared health care policy program, the AOTMiT President's positive opinion on the draft is required. It was indicated that the provisions on qualifying the health service as a guaranteed are broadly applied to formulating the opinion. They could be named as some sort of non-clinical reference standards in the assessment procedure.

15 Transparency council is even mentioned in some scholary works as a seprate body of AOTMiT, even though not indicated as such directy in the act (Pietraszewska et al., 2018: 263).

16 The National Health Fund (Narodowy Fundusz Zdrowia, abbrev.: NFZ) is a main payer in the Polish health care system, a public institution responsible for funding and to a large extent organizing the health care system (Lenio, 2018: 150–151).

Indeed, according to Article 48a.7 of The Act on Public Funding of Health Care Services, the President shall assess the newly prepared health care policy program against all criteria set out in the Article 31a.1 of The Act for the procedure of qualifying the health care services as guaranteed, including the non-clinical ones.

Although the continued and already assessed programs or those basing on the recommendation list for health care policy programmes do not need to be assessed again, they once needed to satisfy the Article 31a.1 conditions – either during the first assessment (the continued programs) or because the recommendations are also based on those criteria[17].

The requesting organizer shall obtain positive opinion or adjust the program according to the positive-under-condition opinion of the President to introduce the health care policy program. Negative opinion compromises the program and ends its existence at the draft stage. As of 30 November 2017[18], potential introduction of negatively assessed program would constitute a violation of public finances discipline, which entails proper proceeding.

So, as an obligatory part of the President's opinion, the non-clinical criteria of qualifying health care policy programs constitute an important factor in the whole set of elements necessarily needed to implement and carry out the health care policy program.

4 Direct application of the non-clinical criteria in assessing the health care policy programs and its consequences to the programs' organizers financial independence

4.1 Direct application of the non-clinical criteria in the assessment procedure

It is remarkable that the legislator did not formulate a directive to apply criteria for qualifying health care services as guaranteed *mutatis mutandis* to the assessment of health care policy programs. The regulation is phrased clearly: 'The opinion is drawn up basing on the criteria referred

17 Article 48aa.2 of The Act on Public Funding of Health Care Services.

18 The Act of 29 September 2017 Amending the Act on Public Funding of Health Care Services and Certain Other Acts.

to in Article 31a.1'. Therefore there can be no modification, let alone excluding some of the provisions.

Focusing on the non-medical criteria, the first of them: the ratio between costs and achieved health results, do not seem to be that problematic. However applying the criterion of financial implications to the health care system, including the financial implications for those obliged to public funding the health care services, raises some doubts, since there is no further clarification of the usage of that criterion in slightly different circumstances in the procedure of assessment of the health care policy programs[19].

4.2 Costs to achieved health results ratio criterion and its application

The ratio between costs and achieved health results criterion is close to the efficiency notion in the terms economic sciences – an indicator of the resulting effects compared to the resources involved (Jastrzębska, 2016: 43–44). It could also be regarded as a premise on the edge of the DG SANTE[20] – determined Rapid Relative Effectiveness Assessment and the Full HTA Assessment (*Inception impact assessment:* 2), except that the legislator rather made an emphasis on the financial efficiency, namely a non-clinical aspect. The connection between this very factor and efficient spending rule in terms of the Act on Public Finance was also emphasised by the legislator on the occasion of the Act on Public Funded Health Care Services (*Bill 1791:* 22–23).

Given this unique position on the verge of two 'measure' groups, the direct application is feasible and poses no problems. The health care policy program is by the definition an action on providing specified health care service or set of them, put in the frames of public funding[21].

19 The judicature sees content of the rationale as a part of so-called authentic interpretation of law (see for example: Supreme Administrative Court, II OSK 2915/13). As of yet the only hint given by the legislator in this manner over interpretation of the 'direct application directive' comes from Bill 1791: Government Bill to Parliament as The Act Amending The Act of 27 August 2004 On Public Funding of Health Care Services. The bill, which makes the President's opinion obligatory in the procedure of health care policy program assessment, dedicates lion's share of the rationale to the non-medical criteria in connection of the Act on Public Finance (*Bill 1791:* 21–22).

20 Directorate-General for Health and Food Safety of the European Commission.

21 Compare the legal definition in footnote 1.

All in all, among the measures to be taken because of the shortage of public resources, the need of providing efficiency overshadows the others. Taking into the account the already discussed Article 68 of The Constitution, there is literally no difference on this field between assessing health care policy programs and qualifying the health care services as guaranteed.

It is cohesive that the President of AOTMiT is entitled to assess the medical and budgetary interface with support of the AOTMiT as an expert HTA agency. Notwithstanding the decisions of empowered health care policy program organizers, it is thus a clear expert field of action to decide about the medical justification of spending public sources to fund specified technology and to decide whether sufficient funds could or could not be provided for the conduction. And this field by any means is reserved for the President.

In particular, focusing on the specific relation between the health care service and the reason for funding this service *in abstracto* does not interfere with the competences of the program organizers, since it would applicable and valid in any circumstances, no matter which entity would be interested in funding the health care service.

4.3 Criterion of financial implications to the health care system, (including the entities obliged to public funding the health care services) and its application

No further clues for applying latter non-clinical criterion can be found elsewhere, including the *Bill 1791*… or any other sources considered as a sort of authentic interpretation.

In the Polish health care system, it is the dominating National Health Fund to which the rule seems to apply in the first place. In the structure of public health care funding, National Health Fund provides 85 % of the public resources (GUS 2018: 121), overwhelming other public funders, taking into the account 'dispertion' of the local government units[22].

22 Combined contribution of local government units in public funding equals 4 % (GUS 2018: 121) It is virtually impossible to assume that all of the local government units start to coordinate they actions and, additionally, focus simultaneously around one chosen issue.

Because of that, the rule's relevancy is troublesome within the regulation on health care programs assessment[23]. There is no functional match in the aspect of funding between National Health Fund and the entities entitled to carry out health care policy programs. This raises doubts on the actual feasibility of assessing the result of any health care policy program and its impact on National Health Fund, as there shall be little or none.

What is more, there is no functional connection between the entities entitled to carry out the health care policy program themselves. The fields of action and operating ranges, let alone finances, do not overlap on each other in administrative or financial terms. Systemically, virtually no impact on them could be made by one another, since they are on different levels in the structure of the public administration and there is dispersion of local government units.

Actually, when it comes to the minister responsible with health as health care policy program organizer, it is in particular AOTMiT that is overseen the minister. *Inter alia*, the minister appoints the Agency's President. The Agency also submits its financial and activity report to the minister. And since the minister also oversees the National Health Fund and monitors its financial condition, the minister in principle has a better view on the impact of minister's own health care policy program's impact on the National Health Fund.

Excluding the conclusion that the regulation on the second criterion was meant to be null and void, which is inadmissible in terms of the rationale legislator concept, all of the above-discussed issues imply that the application of the criterion of financial implications to the health care system in the process of assessing the health care policy programs is impracticable and useless.

As explained further below, it also constitutes an unlawful interference in the financial competences and independence of the health care policy

23 Although the criterion could be discussed already on the basis of the procedure of qualifying the health care services as guaranteed. Nevertheless, it seems to be quite understandable that while qualifying the health care service as guaranteed, the minister with responsibility for health shall take into consideration the implications of the potential decision on the National Health Fund. After all, the Fund would be the entity responsible for financing the newly qualified health care service.

programs organizers, as there is no competence assigned to the President of the AOTMiT to interfere or meddle in the financial independence of those entities (more on that further in the article). Undertaking the health care policy program is optional and a sovereign, unforced decision of the organizer.

5 Applying the criterion of financial implications to the health care system as a breach of some entities' financial independence

5.1 Criterion of financial implications to the health care system in the context of financial decision-making independence of the minister as health care policy program organizer

The act on Public Funding of Health Care Services empowers the minister to organize the health care policy programs[24]. The minister is a central level one-man government authority and a part of a Council of the Ministers, accountable to Prime Minister (working responsibility), Sejm[25] (political responsibility) and State Tribunal (legal responsibility) (Hauser 2012: 143).

According to the Act on Divisions of Government Administration, minister responsible with health is in charge of health division. For this reason, the minister is also a decision-maker for the budgetary part corresponding with the administrative division[26].

Each of the budgetary parts results from the annual budget act. According to the Act on Public Finance, the decision-makers for the budgetary parts prepare a budgetary draft respectively for each of their parts. Then, when budged act is in effect, the decision-makers for the budgetary parts are responsible for executing the part that they are responsible for, including

24 Even though the regulation does not directly indicate the minister responsible with health, the doctrine tends to equate those two terms (Pietraszewska-Macheta 2018: 440).

25 Sejm – lower chamber of the Polish parliament.

26 And as it was mentioned, the minister responsible with health, performing supervision of the National Health Fund, approves the financial plan of the Fund (in agreement with the Minister of Finance). Thus, the minister responsible with health has 'institutional' awareness of the Fund's financial condition and the public funded health care system financial condition.

breakdown of the resources between subordinate units (Misiąg 2015: 515). The legislative initiative is held exclusively to the Council of Ministers[27]. However the decision-makers for the budgetary parts could make some minor changes in their parts in the executing stage (Cyman 2014: 340–341).

Taking into the account the above considerations, it shall be stated that the application of the criterion of financial implications to the health care system (including the entities obliged to public funding the health care services) by the President of AOTMiT in the process of assessing the health care policy program organized by the minister leads at least to the violation of the minister's financial decision-making independence[28]. Financial resources earmarked for the health care policy programs are budgeted as expenses and as such, according to the Act on Public Finance, shall be done for intended purpose and in due time (Misiąg 2015: 553). Negative opinion of the President based on the discussed criterion, would cause an actual breach of the independence of the minister pursuant to the indicated provisions.

5.2 Criterion of financial implications to the health care system from the perspective of financial decision-making independence of local government unit

The provisions of the Act on Public Funding of Health Care Services empowering local government units to carry out the health care policy programs are in keeping with the laws on the local governments' own tasks in health care (Rabiega-Przyłęcka 2015: 272).

Giving these competences is an expression of the financial independence of the local government units at all levels, embodied in the rights to gather income and decide on the expenses. Hence, financial management of each local government unit is run on the basis of the budgetary resolution (Glumińska-Pawlic 2003: 64–65), proven being an optimal tool of financial management (Bartsits 2018: 42). The local government finances are a part of the public finances, but the decision powers are dispersed as a result of decentralisation (Drywa 2016: 118).

27 Article 221 of the Constitiuton of the Republic of Poland.

28 Obviously, difficulties would show up especially when, basing on this criterion, the President's opinion is negative and thus overthrows the program on its way to legally and factually be carried out.

Therefore, within the law, the local government's spending depends solely on the will of its entitled bodies. Also, any other public authority shall refrain from interfering in those bodies' competences in law making[29] (Salachna 2012: 58). Being a part of public finance sector, local governments are to consider the Act on Public Finance's conditions of managing the public funds.

Local governments are supervised. Since the supervision aim is to provide acting of the local government bodies in accordance with law – including obeying the fiscal rules (Zawadzka-Pąk 2017: 112) – the legality shall be the only criterion applicable[30]. Thus, legal remedies are imminently granted against the illegal supervisory activities (Glumińska-Pawlic 2003: 218). Supervisory authorities are exhaustively listed in the Article 171.2 of the Constitution. The entitled authorities in general do not exceed beyond those mentioned in the Constitution, even though some scholars point also to the parliament and administrative courts as also constitutionally empowered to exercise some control powers (Glumińska-Pawlic 2003: 223).

However, not only is AOTMiT a non-constitutional-ranked body, but also the Agency is not present in the legislation as an entity entitled to interfere with the local government financial decisions and the supervisory body.

Because of that, the Agency's President's right to apply the criterion of financial implications to the health care system in the procedure of assessing the local government's health care policy program is highly doubtful.

Firstly, there is no competence assigned to AOTMiT in assessing the acts of will of the local government on the financial issues. Secondly, even if there was an assumption made granting such competences to the Agency's President, the criterion of financial implications to the health care system by any means would not be a legality criterion – the only permitted one[31].

29 The two signs of independence could also be reffered to as positive and negative aspect of local government independnce (Salachna: 58).

30 See: Article 171.1. of the Constitiuton.

31 In fact, it is a judgmental matter, because there is always a background of other entities in the field of financing the health care system. It is hardly imaginable that those entities would in any case legally interfere with the local government unit as independent health care policy program organizer.

Thus, the opinion of the Agency's President based on the discussed criterion would cause an actual breach of the local government units financial independence, since by law no other health care policy program organizer or any other entity obliged to public funding the health care services could interact with the local government unit independent decision making competences in the matter.

6 Conclusion

The presence of the non-clinical criteria in the Polish legal system is constitutionally justified. As confirmed by the judiciary, the criteria do not conflict the rights of the beneficiaries granted by the Constitution in the mater of access to the health care services. On the contrary, it was proven in the article that they tidy-up the access adapting the shortage of funds to the medical advancement. The aim of the implemented criteria thus was to provide due assessment of the health care services in the procedure of qualifying the services as guaranteed for the beneficiaries.

Since the same non-clinical criteria are referred to in the procedure of assessing the health care policy programs, the above made remarks are also relevant in discussing their presence in this procedure. Thus, their presence in the procedure is justified and seems to target the same aims.

The President of AOTMiT, an expert agency dedicated to HTA in the health care system, conducts both of the assessment procedures. The agency itself is overseen by the minister responsible with health.

De lege lata, the application of the non-clinical criteria in assessing the health care policy programs is to be done directly. This makes each of the criteria to interfere differently with the legal system.

As it was proven, the costs to achieved health results ratio as a first criterion, 'binding' the clinical and non-clinical input data, does not interfere in any way with other legal regulations, as its application seem to be fully understandable in the light of the health care policy programs goals. It is the President of AOTMiT entitled by its position in the system to assess if the intentions of the health care policy programs organizers are in line with medical results gained with particular level of funding of the program.

On the other hand, the latter criterion – financial implications to the health care system (including the entities obliged to public funding the health care services) – seems to be troublesome in applying o the health care policy programs assessment.

Firstly, it interferes in the financial independence of the health care policy program organizers. Hence, the regulations put the President of AOTMiT on a collision course with bodies legally empowered to carry out health care policy programs. The President is not authorised and shall not be granted powers to compel any body entitled to independent financial decisions with the President's decisions reasoning from other entities financial results.

Secondly, the direct application of the criterion directive violates the systemic independence of the health care policy organizers, both on the central level – ministers as the decision-makers for the budgetary parts, and on the local level as well – the local government units, each of them being independent and supervised by constitutionally indicated authorities.

This contradiction could be removed only by changing the law. *De lege ferenda,* some alternative legislative solutions could be proposed: firstly, the non-clinical criteria or solely the second one could be applied *mutatis mutandis*; secondly, the second non-clinical criterion could be removed from application in the procedure of assessing the health care policy programs; last, but not least, a separate set of criteria could be proposed for the procedure of health care policy programs assessment.

Current legal situation is of significant importance in the practical aspect as it may lead to an unlawful interference in the independence of the health care policy program organizers, in consequence blocking the health care policy program to be carried out already on the assessment stage.

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In Search for a Model of State Pension Insurance Financially Viable and Independent of the Central Budget

Tomasz Sowiński

Abstract

The following paper presents, in a nutshell, the history of the efforts undertaken, over a period of more than one hundred years, to arrive at a pension insurance model which, being part of the public social security system, could operate as a scheme financially viable and independent of the central budget. Undoubtedly, the question should be answered whether the pay-as-you-go pension scheme, which forms the basis of the social systems of most countries, should be continued. All the indicators determining the condition of the pay-as-you-go pension insurance model were presented by the author in a logical square model, thanks to which one can get a full picture of his possibilities and shortcomings, especially the latter ones. A plethora of reasons that make solving the problem difficult has been addressed, from axiology to logics to legal environment of public finance, viewed in the local (national) dimension and universally. The dogmatic legal research method and historical approach were adopted to that end.

Keywords: Pension Insurance Schemes; Social Security; Insurance; Public Finance; Budget.

JEL Classification: H55; H60; J88.

1 Introduction

Social insurance is the most popular form of care extended by the state over its citizens. It has been developing for almost 200 years now, although considered as its origins is the German *Sozialversicherung* – the common pension insurance – established in 1889. The three ages of the development, sometimes spoken of, is thus, actually, more like 130 years, spread over three centuries.

At least half of the period was marked by massive efforts of many a country to resolve the numerous ailments of public social insurance system. An essential problem lies with the fact that a majority of the social insurance schemes follow the pay-as-you-go insurance model coming from Bismarck. In the course of time the scheme's basic parameters have undergone such dramatic changes that the system has, in fact, lost the capacity to effectively meet the expectations attached to it, and has become a serious burden to the public finance.

It still has many adherents, though, due to – unfortunately – the absence of an alternative (and, worse still, the lack of enthusiasm to look for it, permanent modifications of the existing system being undertaken instead).

The author believes that, as far as the pension insurance is concerned, the approach taken actually leads nowhere, since the capacities of the pay-as-you-go model of pension insurance are limited by certain ongoing factors which, in practical terms, cannot be further modified.

2 The three centuries of the Bismarckian social insurance

Social insurance is a form of financial commitment of the citizens who, in return for the contributions made, are supposed to be provided benefits determined by the type, nature, amount of the contributions made and the period throughout the latter were paid. With time, the scheme lost its original nature, having overgrown with an enormous number of developments (concerning the performances in particular). Neither is the pooling or resources, managing them and economising on their use – sometimes reaching the point of absurdity – free of frequent interference[1].

According to the classic approach, three methods of implementing social security can be distinguished: care (assistance), provision and insurance[2].

Three types of techniques (or, more specifically – techniques originating in the three various principles: of assistance, insurance and provision) are

1 For a broader discussion see: Sowiński. T., "Podmiotowa koncepcja zabezpieczenia emerytalnego. Studium prawnofinansowe", CeDeWu, Warszawa 2019.

2 These are discussed by many authors. Cf. *inter alia*: Piotrowski,1966: 163; Muszalski, 1999: 84; Kluszczyńska, Koczur, Wróbel, Szpor, Szumlicz: 21; Ofiarski., 2003: 696.

distinguished by J. Piotrowski who, by the way, stresses that the techniques are usually portrayed, as leading principles, in their pure (ideal) forms, unlikely to be encountered in reality (Piotrowski, 1966: 164). The fact is well-worth remembering when individual techniques applied by the state in meeting its social security-related duties are analysed – the approach protects the reviewer against wrong assessment of the techniques, both as far as their entirety and particular solutions employed are concerned.

The first of the above mentioned methods (assistance) is, at the same time, the oldest one. While its origins can be traced back to ancient times, its more elaborate manifestations can be observed in the late Middle Ages, and its particularly dynamic development in Europe falls to the 17th century. The allowances provided, usually very modest, were accompanied by various restrictions of personal liberty. With time, in the beginning of the 20th century in particular, the method in question evolved towards modern social assistance. The new meaning of the schemes owes its shape, to a great extent, to the social teachings of the Catholic Church. These were started by the encyclical (Leon XIII, 1987: 41–67)[3] of Leo XIII[4], titled *Rerum Novarum*.

Social provision, as a method of social security, takes a few forms, among which the original one, consisting in performances being funded from public resources, can currently be distinguished. Under the scheme, the source of the funds for delivery of performances is monies pooled in the central budget. A kind of contributions may also be used in systems following that model, which contributions actually resemble a tax, levied and paid to fund the allowances.

A frequently observed form of social provision consists in granting the right to performance, under specific rules, to selected professional groups; differentiation depending on the types of needs being also practiced (performances on account of the state of health, performances to the handicapped and veterans or allowances paid under special circumstances). These are also provided by public bodies from the budgetary funds.

3 A *sui generis* summary of the content of the earlier social teachings is contained in John XXIII's *Pacem in terris* encyclical, which draws attention to the necessity of guaranteeing to people financial resources necessary for a dignified life, including social benefits.

4 See, more broadly, the Rev. I. Majka: (Majka,1986: 331, 332).

The third, insurance-based method, is the most widely employed one, although it, too, has lots of forms and involves various detailed solutions. Considering the need to secure the funds for payment of the pension benefits, an opinion is voiced that "*insurance is, as a form of organisation of a relevant fund, the best scheme from the technical point of view*" (Goronowski, 1961: 305.). The view meets with criticism ever more frequently.

It can, however, be safely assumed, that a majority of the forms of social insurance originate with either of the two ideas the insurance is practiced in, discussed further on, or refer to at least one of them.

One of the ideas in question is the idea of the so-called Bismarckian insurance, based on the relationship between the insurance and employment, with proportionately set contributions and pensions linked to the amount of wages. It is open to the operation of non-governmental institutions, as regards maintenance of the level of income and the securing of due standards.

The other one is the Beveridge model, characteristic of which is the universality of insurance categories. Following that idea, the state aims at creating a model of insurance supposed to provide means of subsistence, calculated at a level satisfying minimum needs, to possibly widest circles of the society, upon their reaching the retirement age. The source of the funding is taxes or contributions of a nature similar to taxes. A possibility to obtain performances exceeding the minimum is left by the state to the individual foresight of members of the society. Legal framework for such undertakings is often established, though. Most often encountered are the so-called occupational pension schemes.

Both solutions have evolved over time, the available options being further enhanced. Based on them, mixed solutions were being established as well. It can also be seen that some of the original differences between the two solutions became blurred, subsequent versions of national pension models and systems taking shapes ever more similar to one another (drawing inspiration and ideas from other countries that implement them is, after all, only too natural in the era of globalisation). The three-pillar (three-tier, three-span) system happens to win particular popularity in that respect. Pillar one is assumed to secure the basic minimum retirement benefit, usually

guaranteed by the state itself. Funded under the PAYG (Pay-As-You-Go) system, and being also referred to as the solidarity benefit scheme based on an "intergenerational agreement", the solution consists in the pensions being paid from the funds contributed by the working generation. According to the "agreement" in question, after having reached the retirement age, the generation in question should receive their performances from the generation next in turn. Calculations for the system are made in short periods, a span of one-year considered to be that basic. Pillar (tier) two, mandatory for all those employed, is expected to provide an additional, supplementary part of the performances and is based on pension funds managed by private entities. Pillar three should secure at least safety and a real rate of return on the pooled assets

The benefits of the three-pillar system can be considered in many aspects; the Swedes have even dubbed it an "ideal account". It limits the negative effects resulting from demographic changes and not only does it not entail any transformation costs during the transition period but, actually, can significantly reduce them. In addition, the scheme also mitigates the risk of social aspects dominating over the economic ideas, and – last but not least – stimulates the individual responsibility, prevention and activity of the insured.

The insurance method, regardless of the adopted legal architecture, is almost universally employed in modern social security systems (including pension schemes, as the systems' most fundamental part). Some of its solutions, those applied under the third pillar concept in particular, make it close to business (commercial) insurance, especially life insurance of a commercial type. A few essential differences between social insurance pension schemes and business life insurance can, however, be named. First of all, the former one is mandatory, general in nature and the performances provided by it are usually state-guaranteed. Regardless of the financial and legal architecture, the financial resources used to fund pension insurance are pooled and managed by pension funds.

Under insurance systems autonomous funds are sometimes established for the pooling of revenues coming from contributions and from other sources. It is from the monies accumulated in them that the performances payable

in the amounts stipulated by law are provided. Such funds are usually established separately for specific types of social insurance allowances and are managed considering the nature of respective payments. This means that in the short-term insurance income and expenditure are balanced under the annual apportionment scheme, whereas in long-term (retirement) insurance, reserves to balance the future increase in expenditures are formed and invested in a way that ensures their capitalization. Managing them should be based on the principles of strict calculation of current and expected revenues and expenditures and controlled using actuarial methods – the insurance calculus (Social Security, ILO, 1958: 104–107).

In the post-war period (i.e. the latter half of the 20th century) there was a general retreat from capitalization to the pay-as-you-go solution, with the apportionment made within not too long periods (several or at most ten-year long ones).

Solutions like that resulted in the need to periodically review the assessment of contributions and the level of other income. Accumulation of long-term reserves was not necessary, though. This did not remove the need to carefully calculate income and expenditure and control the actual level thereof, as compared to the expected one. The calculus was made within the periods that could be covered by a relatively accurate forecast, supposed – in principle – to significantly reduce the risk of unpredictable disruptions. This way of organising and financing pension insurance raises, however, a problem of providing subsidies to the pension funds from the budget system. Much larger perturbations occur as a result and, in addition, the problem becomes politicised. Under the pay-as-you-go scheme, the periodical review of the balancing of income and expenditure should be based on a precise calculation taking into account a whole array of factors, such as: the level of wealth of the society (and its growth) and thus higher expectations regarding the size of benefits, the average life expectancy, the development of the labour market, the proportion of employees to those eligible to receive retirement benefits etc. The last several decades reveal a steadily growing trend of all the indicators and a decrease in the ratio of the size of the working group to those entitled to receive the pensions. As a result, the decision-making bodies are forced to revise the basic criteria and principles of retirement insurance

every ten years. The simplest solution is then to increase or at least maintain the relative amount of benefits and the category of persons entitled to them. It involves a necessity to increase budget subsidies or insurance contributions and to extend the period of employment making one eligible for obtaining the retirement benefits.

Abandoning the changes usually entails limitation of the volume and amounts of retirement benefits. Both solutions are hard to implement, though, given the problem of the budget system solvency and social discontent. Alternative solutions unfortunately result in the permanent increase of the burdens weighing on the central budget, on the one hand, deteriorating the situation of the beneficiaries on the other. Attempts to untangle the Gordian knot have been taken at least since the 1970s, in a variety of ways. Regardless of the proposed solutions, opponents to the proposed concepts always abound. Therefore, no universally recognised patterns have been worked out, there being always advocates of the pros and cons of the more or less comprehensive solutions emerging in the course of the work.

The search for a new form of social insurance, done in recent years, resolves itself to making economies in the system of social insurance. The solutions adopted as a result are, at times, truly incomprehensible and bring about losses rather than the benefits hoped for. Social insurance models are based on a *sui generis* self-financing by the insured themselves (Sowiński, 2018: 604). It is from there that the idea of social insurance solidarity is derived, consisting in the pooling of resources for future pension benefits, usually distributed disproportionately. The latter trait is caused by, first of all, the intention to provide at least minimum payments to those receiving least, by a great number of seemingly fair (if not outrightly humanitarian) indications taking into account "higher" reasons, by numerous privileges characteristic of certain periods in the development of specific societies or simply by the ideology prevailing at a specific place and time. Added to that should be the solutions which can hardly be explained other than by the existence of a despotic will of the oligarchy ruling (not quite democratically) the country, no matter how heavily is the financial condition of social insurance affected thereby. A good example of the above is the status of the uniformed services, not paying insurance contributions in the Polish People's Republic

(as was Poland dubbed under the communist rule), while it was them that enjoyed the greatest number of pension-related privileges during that time.

The social security system is not homogenous; it is also complicated as regards its legal and technical architecture, based on regulations reckoned towards a few branches of law. That truth should be remembered when past and contemplated reforms of specific parts of the system are being discussed – temperance should be the virtue when both criticism and positive opinions are voiced on the subject (Jończyk, 2011: 10).

Considering the above, the view that the experience of the private insurance sector should be made of in the public system happens to be expressed by many a representative of the academic world, the economists in the first place.

3 Private or social insurance?

The division of insurance into business (commercial) and social is widely recognised, even if the division itself and the adjective "business" in particular, do not seem to be wholly appropriate. More reasonable seems to be splitting insurance into that private and public, and making a division into voluntary and mandatory insurance would not be wrong, either. Such an approach is, however, definitely much harder to justify and win social acceptance. The term "social insurance" sounds friendly and the mandatory nature of the scheme can be easily justified using high-flying slogans, often supposed to hide the fact that the solutions themselves (and the ways in which they are introduced) are far from social expectations.

Personally, the author would welcome, following the Ulpian's division of law, a split of insurance into private and public [assecuramentum privatum – assecuramentum publicum], but – understanding complexity of the problem on the public side and the deep engraving of the term "social insurance" in public consciousness – proposes viewing the division as made between private and social insurance[5] (provided that the latter is arranged keeping in mind the welfare of the society, no political or economic goals being pursued). It is well-worth noting that whereas the term of office

5 Regardless of the said, in the course of further consideration, the traditionally recognised division shall be followed to avoid additional, unnecessary confusion.

of a government or the legislative authority does not exceed, in individual countries, 4–5 years, the assessment of the efficiency of social insurance schemes must take place in the perspective of 2–3 generations, i.e. in a period of 40–60 years. This should inspire respect to institutions and, consequently, humility of those eager to make any changes in them.

Issues that should be emphasised include: the private nature and voluntary conclusion of insurance contracts in the private sphere, as opposed to the public and mandatory character of social insurance schemes.

The state, and – on its behalf – specialised (usually public) institutions, manage the resources of those insured. Mandatory nature is one of the main traits of social insurance. It is manifested in what the literature calls automatism, equated by some authors with the arising of the insurance relationship ex lege (Liszcz, 1997: 23 i 24) or with independence of the relationship from its parties (Warkałło, 1974: 173). That feature is additionally enhanced by the lack of an insurance agreement. Under pension insurance the arising of the legal relationship is thus automatic and comes by operation of law, which can be viewed as a consequence of the mandatory character of the insurance, resulting from its structural principles. It is, in particular, C. Kosikowski who, when discussing the arising of a mandatory insurance relationship, stresses that is emerges ex lege, as soon as relevant requirements provided for by the law establishing the relationship have been met; this in, fact, the above discussed situation of the insurance relationship arising automatically (Kosikowski, 1986: 188).

Under the pay-as-you-go model of pension insurance, the resources pooled are those supposed to be employed during a specific year. The source of the funding of the payments is current contributions (plus the subsidies and donations, if any). The funds pooled are ones to be spent. Through the applied scheme a cross-generational redistribution takes place, the working generation funding the performances to persons at the retirement age.

Under the capital funded model the resources accumulated by the insurer are equal to the capital value of liabilities. The contributions brought in are lower than those paid under the pay-as-you-go funded scheme, as they are decreased by the amount of the interest accruing throughout the period of duration of the insurance. The thus collected funds are ones

of investment nature and have, in fact, to be invested in an income-generating way. The financial operation of social insurance is then based not only on contributions but also (at least to a considerable extent) on income gained on equity instruments (Majchrzycka-Guzowska, 2002: 192). A solution based on current financing of social security benefits (including pension benefits) from budgetary resources, that is from resources obtained mainly from taxes, is also admissible.

The retirement benefit does not result directly from the contribution, but a certain interdependence between them can be spoken of, since the contribution is determined as a percentage of the income obtained. In order to calculate retirement or invalidity benefits, earnings are also taken as the basis. That type of relationship, though not taking the shape of a mathematical formula or direct transfer, is, however, noticeable (Sowiński, 2009: 95–96).

According to M. Góra both models are parts of institutionalised solutions. Both are mandatory and the only difference between them lies in the way in which the financial resources to finance future retirement benefits are generated. As regards the pay-as-you-go model, people are obliged to pay the contributions from which the funds for the payment of retirement pensions generate. Under the capital funded scheme the public is forced to repay, from the preceding generation, the assets mandatorily brought in by them in the period of their being economically active (Góra, 003: 42).

The author does not fully share the above quoted opinion. In fact, the success of the capital funded model (i.e. attracting the funds for the performances to be paid) depends on the purchase of the assets held by the insurers, yet no "forcing people" (the next generation) to buy them may be talked of. The assets, taking the form of various securities and investments are subject to the general market rules. Not only there may be no need to make anybody acquire them, but the assets are likely to be most desired investments, the buyers expecting them to be highly profitable. As regards bonds, they are redeemed by relevant institutions having achieved their goals through the issue of the securities, which goals – in the case of public entities – are also socially beneficial. It is just what the insurer's task consists in, viz to skilfully invest the monies of the insured and make them additionally grow thanks to the operation of the free market game rules. No forcing people

into buying securities is thus contemplated! This is a most essential (though usually neglected) difference between the mandatory and voluntary (the pay-as-you-go and capital funded) schemes.

Regardless of the way in which the financial resources for payment of future retirement benefits are generated, the goods consumed by the generation of the retirees must be produced by the working generation. The key role under the pay-as-you-go model is played by political decisions.

Under the capital funded model the obligations towards the retired are more clearly defined, much stronger and provide a better guarantee of payment of the benefits (Sowiński, 2018: 614).

4 The search for an appropriate model of social insurance in the 20th century

At the end of the 20th century the "development" of social insurance systems consisted mostly in permanent reforms of the latter. The scope and shape of the reforms, just like the willingness to find new solutions varied greatly across the countries. In wealthier states and societies these were carried in a peaceful atmosphere and cautiously. In the less affluent countries fighting with the crisis of public finance (or even undergoing the stormy time of political transformation) the changes were dramatic, if not openly revolutionary.

The most widely known – and commented on – pension insurance reforms were undoubtedly those effected in Chile and Argentina. Put to reforms were also pension systems of countries of the Indian Ocean Region and those of the Eastern and Central Europe. The most characteristic, as regards the latter, were the reforms undertaken in the Czech Republic, Hungary and Poland.

In each situation the reforms of pension systems were caused by, first of all, financial reasons and were designed to help achieve financial viability of the schemes. They were, however, undertaken under widely differing socio-economic and political conditions and, consequently, varied greatly in terms of their nature and shape. Europe would reform its pension insurance systems while enjoying social peace and welfare, with forecasts

covering a span of 20 or even 30 years. Meanwhile, reforms effected in the countries of the South and Latin America in general[6] took place under extremely tough social and economic conditions, with state financial systems collapsing and social unrest being often present. The countries became a kind of a "testing ground" for various ideas of how the pension insurance system should be organised and funded, put forward by scholars of the Western Europe[7] and America[8], as well as the World Bank experts[9], in whose opinion the schemes implemented in the Latin American countries aimed at introducing legal and financial arrangements, with the value of the future pension benefits being "covered" by the invested assets. The reforms may lead towards the pension insurance paradigms being now in force (Schermers, 1998: 9 and others).

The reforms undertaken in countries of the Eastern and Central Europe were carried out in a very difficult situation. After a long time of existence of the socialist system, with economic processes being centrally managed under what was termed the planned economy, the countries found themselves on the verge of bankruptcy. The situation was dramatic in that the countries had to face huge public debt, limited markets and the overgrowth of a "manually operated" (as it was referred to) social policy with

6 The pension system, as existing in countries of the South and Latin Americ, is discussed at length by: Sowiński T., Capital Funded Models of Pension Insurance on Selected Examples Part 1, Financial Law Review, University of Gdańsk L Faculty of Law And Administration, no. 1 (4)/2016, pp. 1–14. Available at: http://www.degruyter.com/view/j/flr, Unauthenticated Download Date |7/17/17 10:44 PM, and Capital Funded Models of Pension Insurance on Selected Examples Part 2, Financial Law Review, University of Gdańsk L Faculty of Law and Administration, no. 1 (4)/2016, pp. 15–26. Available at: http://www.degruyter.com/view/j/flr, Unauthenticated Download Date | 7/17/17 10:46 PM.

7 See, among others: European Social Policy – A Way Forward for the Union. A White Paper, COM (94) 333, consolidated text of 27. 7. 1994; A Report by the Social Protection Committee to the Göteborg European Council on the Future Evolution of Social Protection 2000.

8 More broadly about the pension system of the United States of America, cf.: Sowiński T., The pension system of the United States of America. Selected legal and financial aspects [in:] The Financial Law towards Challenges of the XXI Century, Michal Radvan, Jolanta Gliniecka, Tomasz Sowiński, Petr Mrkývka (eds.). Publications of the Masaryk University, theoretical series, edition Scientia, file no. 580, Brno Masaryk University, 2017.

9 The report can be found in the document: Averting the Old Age Crisis: Policies to Protect The Old and Promote Growth, World Bank 1994.

pension payments usually depending on the current condition of the state budget. In combat with hyperinflation, the rules of management of the economy and public finance were being changed. A challenge to the states in question also consisted in the problem how to establish entirely new regulations in the field of pension insurance and develop a fresh, coherent idea of the operation of a broadely termed social security system (Sowiński, 2019).

Striving towards the autonomy of insurance funds and abandoning the budget-based methods in management of social insurance systems (Wantoch-Rekowski, 2001: 86) was a marked trend in the reforms of the social insurance systems in the countries of Central Europe in the 1990s. It was believed that creation of earmarked funds would ensure continuous and sustainable funding of pension insurance performances and that separation of the income for the funds would underscore the importance and prestige of the public tasks discussed here (Owsiak, 2000: 131). Moreover, the changes meant a shift from the financial system of social insurance based on the budget (or budget-and-funds) to the fund-based system (Mienicki, 1990: 25), believed to be, as already mentioned, a more autonomous one. L. Mackiewicz-Golnik adds another argument, essential for the management of resources of the pension fund and speaking in favour of its separation from the state budget: the legal possibility of using the reserves of the fund after completion of the budget year in which the reserves were created (Mackiewicz-Golnik, 1989: 287).

Each of the Central European or Latin American countries was subject to different conditions and had different traditions regarding its social sphere Policy. Each of them also had a specific socio-economic situation. All the countries had to develop optimum methods of their own and find the solutions which suited them best and were most likely to succeed (given conformity with the economic environment of their operation). The EU Member States transform their pension systems in an evolutionary way. They also attempt at harmonising the systems (Sowiński, 2019).

5 Is financial autonomy feasible under the pay-as-you-go pension model?

In all reforms effected at the end of the 20th century persistent efforts to secure financial autonomy, or – putting it simply – financial viability of pension insurance schemes can be observed (Sowiński, 2009: 285).

From the economic point of view the common, mandatory pension system is a "necessary evil" *justified only by the social goal it is supposed to attain,* a replacement of the mandatory pension system by a voluntary one not being a resolution to the problem, as it would mean abandoning the achievement of the social goal for which it was established, while those insured, as M Góra puts it – "*do not have real reasons to feel robbed*".

The room for a manoeuvre is therefore very limited and amounts to balancing between the highest possible contribution size (not overweighing the employee and the employer, though) and the possibly low but not demeaning amount of pension benefit.

Unfortunately, the creation of a duly functioning pension system does not consist, to say it vividly, in making a house of Lego blocks, following the attached precise instructions. It resembles more of an attempt to build a palace using the material coming from demolished farm labourer quarters, undertaken by a casual team of people none of whom holds the licence of a construction designer or builder.

Should demographic problems and a rapidly progressing decline in the generational replacement rate be added to the above picture, the palace to be erected is likely to become a house of cards (coming from various decks, to make the matters worse) (Sowiński, 2019).

The conditions ideal for the operation of the pay-as-you-go pension systems can be presented as a set of four factors (specificities, recommendations) put together to form two pairs of opposite qualities:

- 1A. a long period of working career (meaning early entering the labour market and late retirement).
- 1B. (possibly not too long) period spent in retirement.
- 2A. high contributions made to the pension system.
- 2B. a small amount of the pension benefit received.

A precondition for the success of the model is an additional, fifth factor (ratio) – the replacement rate. In the case of search for the ideal conditions of the pay-as-you-go scheme, a high replacement rate is supposed to be generated by a high population growth.

Summing up the "ideal" conditions of the pension system in question, it should be indicated that the citizen ("beneficiary" of the model) is expected by the state (those governing the pension scheme): to work long, pay high social insurance contributions, stay in retirement briefly, receive low pension benefits and have lots of children in addition.

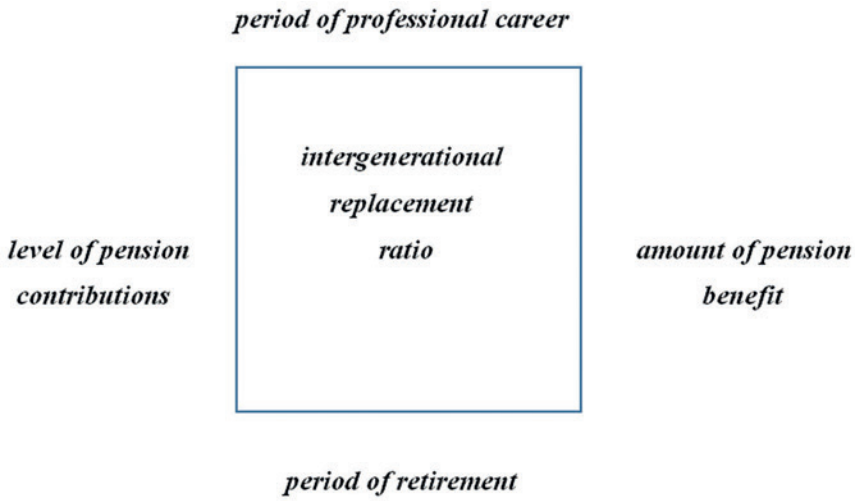
It thus has to be observed that:

- Re. 1A. a long period of professional career means early entering the labour market, i.e. the loss of a carefree childhood, an early start of education, and the late retirement age entailing a higher degree of exhaustion of the stamina (abulia, prostration, various dysfunctions).
- Re. 1B. the (possibly not too long) period spent in retirement, resulting also from the high retirement age threshold, means a shorter period left to enjoy the autumn of life. Naturally, it must not be lost of sight that the average life expectancy has markedly increased since the late 19th century, but the continuous extension of the period of professional career by raising the retirement age results in people being retired for a much longer time, though in worse shape. Figuratively speaking, those insured under the pay-as-you-go funded pension scheme have to work during their autumn of life (at least the most attractive part of it) and it is only the end of the autumn and the winter of life (frosty at times) when the retirement can actually be enjoyed.
- Ad. 2A. high payments to the pension system mean high labour costs, lower net remuneration and, consequently, reduced living standards.
- Ad. 2B. a small amount of the retirement pension results in poor living standards when in retirement and a need for having an additional source of means of subsistence, e.g. some extra job.

The fifth factor (ratio), i.e. the high replacement ratio, achieved thanks to a high birth growth, is bound to be needed at a sufficiently high level

in the future (if not even higher than that starting). The question is, how high is it likely to be after a few generations?

Fig. 1. The square of opposition in the pay-as-you-go pension model



Source: own elaboration

According to the logic of the above square, under the pay-as-you-go funded pension scheme a change in any of the factors brings about a need to change another one (if not all of them), in order to retain the *status quo* of the model. If no decision to change them is made, the only solution intrinsically related to the funding of the scheme lies in providing funds from the state budget. In the long run, however, such a move entails the threat of a crisis in public finance or even a failure of the central budget.

Yet, given that over the span of at least two generations all the factors have undergone many modifications (adopted in the spirit of "optimisation", reform of the system and solidarity of the insured), the room for manoeuvre has shrunk, in practical terms, to zero and any subsequent change requires sophisticated acrobatics to justify it. The reason is always the same, though, and boils down to the lack of financial resources within the operating pay-as-you-go funded pension insurance model.

Serious consideration needs to be given to the fact why – despite the awareness of the obvious exhaustion of the capacities of the model – no efforts were undertaken to develop a new scheme based on other foundations and logic than the system in question. It seems highly likely that the situation results from a heavy exposure to "*virus bismarcosis*", additionally enhanced by absence of ideas how to provide funding in the transitory period.

Whatever these (and probably many other) reasons might be, the inaction of those responsible for the operation of public pension systems (including a search for new models that would be capable of bearing the burden of the financial needs and social expectations) is hard to accept.

Taken together, the above considerations mean that in the pay-as-you-go pension insurance model, the human being is treated like an object, as a "beneficiary" of the model. Such a perception of the system's role and tasks and bringing the person down to the level of a long-lived android, intensively exploited before the short period preceding akinesia, hardly deserves acceptance.

This sound horrible, looks even worse and – considering the approach taken to the people – makes it reasonable to ask a question what the reasons for the existence of public pension systems generally are.

According to the official declarations, the systems are supposed to guarantee to the society a high-standard (or at least dignified) life upon reaching the retirement age. Considering, however, the subsequent amendments made to them, in the countries of modern Europe in particular, a recurrent observation is that the situation is exactly the opposite. It seems that individual countries have got so heavily entangled into the unsolvable problem of handling the hitherto existing pension systems that they try, first of all, to get rid of or at least reduce the issues of solvency of pension funds (i.e. the public costs of running them, the budgetary subsidies in particular) at any price (at the expense of the now working citizens in particular).

The question thus reads: is the human being, referred to as the "beneficiary" of the systems, the focal point of the pension models proposed now, or is he/she just their object, not necessarily the most important one?

Yet another problem is that the search for a new model of pension insurance, despite the lapse of more than fifty years, has not led to development of another conceptually fresh solution, the proposed ones remaining within the circle of the Bismarck, Beveridge, private (capital funded) schemes or compilations thereof. Neither have any ideas for the transitory period been voiced, which makes taking any decision even more difficult; this is particularly true as regards the most important one, that of abandoning the pay-as-you-go model.

Without any doubt whatsoever, a considerable role in that respect is played by the *virus bismarcosis*, or "*the inability to think in categories other than those following from the idea of social security based on the pay-as-you-go concept*" (the pension insurance in our case). The only way of getting rid of it is the undergoing a "drug addict treatment", as it were. No qualitatively new solution that could be a genuine and realistic alternative to the existing ones is likely to be developed without it.

The new scheme must be sufficiently coherent and independent of the system of public finance to survive in modern – complex and volatile – financial market for at least next 130 years (Sowiński, 2019).

If its introduction is not going to pose a permanent threat of a budget deficit, enhanced inflation, increase of state public debt and insolvency of the public finance system, the system is likely to be a truly independent one. If, in addition, a socially acceptable and economically viable solution to the problem of the transitory period can be proposed, the scheme has a chance to succeed. This would also mean a perspective of resolving, if only in part, the public finance problems present in a majority of the countries where the pension insurance models are based on the pay-as-you-co concept and where the numerous attempts to refine it and make more friendly to state budgets always hit the walls of the square of opposition of the pension insurance model existing now.

The issue to be discussed next should thus be one of a person-centred idea of pension security. This, however, requires paying to it, separately, special attention.

6 Conclusion

Looking for a model of public social insurance, financially viable and independent of the state budget, countries of Europe and almost the entire world have already done much. North America sees a growing number of diversified solutions that can be implemented within the framework of public pension insurance. In South America (and Polynesia, by the way) methods of private pension insurance have been adapted to the needs of the social insurance schemes. Lots of interesting solutions operate in Asia, though it is rather difficult to find ones essentially different from those known in Europe and on other continents.

In Europe, the cradle of public social insurance (including the pension insurance touched in this paper), almost the whole 20th century and the beginning of the new millennium were spent in search for a new formula and new funding sources for the public social insurance. Recognised as a matter of utmost importance has been making social insurance independent of the demographic problems. While supposed to be the way towards development of a financially sustainable pension scheme model, the issue were usually circumvented rather than attempted at solving.

Unfortunately, both when proposing new (or, putting it more accurately – amended) solutions and when assessing them, the limitations of the square of opposition of the pay-as-you-go funded system have always posed a challenge, additionally enhanced by the raging *virus bismarcosis*. This is why, 130 years after the establishment, by chancellor Bismarck, of the *Sozialversicherung* – a common pension insurance based on the cross-generational distribution of financial resources pooled in public insurance funds – despite the unimaginable development of science, technology and space exploration, mankind has failed to find an idea for another, based on different principles and other funding sources and methods, model of pension insurance that would stand a chance to be neutral to the budget, independent of inflation, national debt or solvency of the public finance system. The opinions voiced have stated, at the most, that the enterprise was not feasible, or experts were just silent on the issue. And yet, according to the author, the search for a pension insurance model, financially viable

and not burdening the budget is likely to end with a success provided that the legal and financial architecture created is based on the axiological foundation of a new concept, independent of the factors of the logical square of the pay-as-you-go pension model.

In this situation, in order not to leave the reader of the paper with overly pessimist conclusions, the author suggests to take, as the object of further discussions, the issue of a personalised concept of pension insurance.

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Evolution of Public Finance in the Czech Republic

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Abstract

This contribution deals with historical view on public finance in the Czech Republic. The main aim of the contribution is to confirm or disprove the hypothesis that virtual and reality conception of public finance differ. Description, analysis, comparison and synthesis are used for writing this contribution. Novelty of this text is that public finance is analysed from a virtual and real point of view. The reality concept includes the evolution of state and society approaches to public finance. The virtual concept involves the evolution of the term "public finance."

Keywords: Public Finance; the Czech Republic; Evolution; Virtual Concept; Reality Concept.

JEL Classification: H2; H3; H5; H6.

1 Introduction

The idea of dealing with the evolution of public finance has been discussed by the authors for several years. The need for knowledge of public finance, including tax issues in the current concept and the assessment of developments in relation to constantly changing political and economic market situation, has proved to be absolutely necessary.

Public finance is an often mentioned term in theory and praxis, which appears in all states and in different historical times. It is obvious that every

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state needs public finance for the realisation of its activities but the approach to public finance changes in time and with political parties. Public finance is an interdisciplinary topic; it is interesting for lawyers and economists as well. For this reason, it is inadequate to analyse it only from one or the other point of view, as often seen in many publications.

Public finance is a widely discussed topic not only at the level of public economy and politics, but it also has a significant impact on business processes that need to be constantly responded, particularly in the context of current globalisation or recently debated post-globalisation. Thus, the position of public finance in the economy must be gradually mastered both by the representatives of the theoretical sphere and the corporate practice. Of course, public finance is not only dealt with at the level of the Czech Republic, but it is also influenced, inter alia, by consolidating Europe's position as a single unit.

Polish theorists Salachna and Tyniewicki (2017) reflect the impact of substantial transparency on public finance. The goal is based on question how the public authority should inform citizens on the process of collecting and spending public sector income. According to them, principle of substantial transparency of public finance has been inadequately implemented and it might be incomprehensible from the social addressee's perspective. Zalcewicz (2017) stresses stability of public finance. According to him, legal solutions is not warranty for protection against over-indebtedness of municipalities.

Our contribution offers an economic and legal point of view on public finance and is supported by the research project Evolution of legal aspects of public finance in selected countries. The novelty of our contribution is that it offers a new view on public finance in the Czech Republic. Public finance is analysed from a virtual and real point of view. The reality concept includes the evolution of state and society approaches to public finance. The virtual concept involves the evolution of the term "public finance."

The main aim of this contribution is to confirm or disprove the hypothesis that virtual and reality conception of public finance differ. It is possible to state a partial hypothesis to this main hypothesis: economic view

on public finance is more detailed than enacted public finance. Description, analysis, comparison and synthesis are used for writing this contribution.

2 Virtual conception of public finance

Virtual conception is based on analysis of evolution terms of public finance.

Vencovský F. (1994) states that the first definition of public finance in Czechoslovakia after 1918 can be divided into three streams. The first author is Alois Rašín (the first Minister of Finance) who requires a balance of income and expenditure and a minimum range of budgeted revenue and expenditure. On the contrary, Karel Engliš believes that public finance must take into account civil solidarity and public spending should be spent according to social needs. The third stream is represented by Czech Keynesians (Josef Macek and Jaroslav Nebesář). They add that public finance is supposed to replace the lack of private investment and should be realised even at the cost of government debt.

After 1948 and based on the Soviet model, public finance was perceived as state finance which is based on a central planning mechanism, with public finance providing rather record-keeping function.

From the 60s, the term "fiskalita" or "parafiskalita" has been used for public finance. "Fiskalita" meant public finance in the sense of the word and "parafiskalita" was used for public enterprises. Libnar and Špaček state that public finance is based on a central plan and insufficient public revenues are to be balanced by the emissions of the currency.

After the revolution in 1989, the perception of public finance returns before the Communist era and is complemented by the latest insights from market-developed economies.

According to Beneš et al. (1993), public finance represents monetary relations which mediate the creation, distribution and use of monetary funds by the state authorities, local authorities, state enterprises and other public organisations.

Tuček (1995) states that public finance is understood as the sum of the state's finance and public self-governing unions, sometimes including the finance of some state-owned enterprises.

Hamerníkova and Kubátová (1999) are of the opinion that public finance is "*a more modern term, used to identify specific financial relations and operations in the economic system between authorities, public administrations and institutions on the one hand, and the other entities on the other, i.e. citizens, households, businesses, non-profit organisations, etc.*"

Šelešovský (2003) states that public finance can be defined by extending the general definition of finance, i.e. the monetary relations arising in connection with the creation, distribution and use of funds.

From a different point of view, the public finance is defined by Liška and Kubátová (2004: 479) who emphasise the use of public finance as a tool to fulfil the basic functions of the state: "*a modern state as a social institution performs a wide range of functions and in order to fulfil these functions, it must have its own funds. We call these funds public finance.*"

Mrkývka (2006) also offers an interesting definition. Public finance is related to financial law and can be understood as social relationships which arise and are implemented during the creation and use of monetary funds. These funds concentrate public money, they are created in public interest and they are supposed to meet public needs.

Dvořák (2008) presents two perspectives on public finance: normative and positive. The normative view emphasises the societal need for public finance which is derived from the economic necessity of public sector existence. The positive view of public finance is based on the knowledge of the theory of public choice which makes a significant contribution to the critical view of government interventions in general and, of course, in the fiscal sphere. It is thus possible to incorporate it into a broader stream of government failure theories.

Ochrana et al. (2010) look at public finance so that they are part of the public sector and are included in the scientific disciplines of economic theory, financial theory, and financial theory of the public sector.

Peková (2011) briefly states that public finance deals with how to obtain the necessary funds and use them effectively to finance individual types of state interventions.

Bakeš (2012) notes that public finance can be defined as "*the sum of monetary relations related to the creation, distribution and use of the money mass and their parts in entities and bodies of the public sector*."

The latest definition is offered by Maatyová et al. (2015). Public finance does not examine societal problems, but only a certain part of it – namely economic problems and a problem that concerns public funding issues.

If we would like to synthesize the above-mentioned definitions, then the following three groups will arise:

1. Quantitative view – definition based on determination:
   - List of entities handling public finance (Tuček, 1995).
   - List of scientific disciplines which are part of public finance (Ochrana et al., 2010).
2. Qualitative view – public finance functions and public finance requirements:
   - Funds used to fulfil the basic functions of the state (Liška and Kubátová, 2004).
   - Social need for public finance, although associated with government failures (Dvořák, 2008).
   - Efficient use of public funds (Peková, 2011).
   - Economic problems related to public funding (Maatyová et al., 2015).
3. Definitions highlighting public finance relations:
   - Monetary relations (Beneš, 1993, Šelešovský, 2003, Bakeš 2012).
   - Financial relations in the public sector but also in the private sector (Hamerníková and Kubátová, 1999).
   - Social relations related to public funds (Mrkývka, 2006).

Based on the analysis of the theoretical approach to public finance, it can be concluded that this has changed considerably. Although we have focused mainly on the description of definitions that have emerged in the last 30 years, there is a noticeable difference between the concept of public finance definition before World War II, the Communist era, and post-revolution. In the period between the world wars, particular emphasis was placed on the requirements for public finance (equilibrium, solidarity and support for economic growth). In the second stage, it performed only the record-keeping

function of the public sector. The third stage is characterised by the fact that it is possible to meet different definitions. Primarily, it follows the tradition before World War II (qualitative view), however, it is also possible to meet a quantitative perspective and finally, a number of authors look at public finance as the relationship between various entities that are linked by public resources.

If we look at how public finance is understood by the law, then the definition can be found in Act No. 320/2001 Coll., on financial control in public administration. The basic terms are defined in § 2 which states that for the purposes of this act, public finance means public revenues and public expenditures. As seen, this act defines public finance in a very ambiguous way and leaves it to the experts, particularly in the field of law or economics, to further develop aspects related to public finance.

3 Reality of public finance

One hundred years of independence can be divided into six sections according to the main political or economic changes that occurred in the country.

3.1 1918–1925

Macro conception is based on an analysis of the evolution of state and society approaches to public finance. Budget finance is in the first years connected with public finance.

According to History of the Ministry of Finance of the Czech Republic, the newly created state of Czechoslovakia adopted many rules from the Austro-Hungarian Empire. The first budgetary rule was adopted in December 1918. It was Act No. 95/1918 Coll., on budget makeshift. The Government of the Czech Republic could levy taxes with valid rules. The first state budget was adopted in June 1919 with Act No. 433/1919 Coll. and it was based on two principles (according to Alois Rašín): work and economy. The state budget in 1919 was drafted as deficit (revenue about 6,7 billion CZK and expenditure about 10,6 billion CZK).

This situation did not change in the first years; state budgets continued as deficits. There were many reasons: (consequences of World War I and

the consequences of monetary policy). The first surplus occurred in 1925 and related to economic expansion.

The first half of the 20s was characterised by the coordination of state budgets with reality which often led to changes in their structure. The budgets could be common and capital, regular or irregular. At the end of this period, the state budget was divided into current and capital budgets. These changes did not help to improve public finance; for this reason, it was necessary to change the budget system and create independent monetary policy (Vencovský, 1997).

The first period is characterised as follows:

- Interconnection of fiscal and monetary politics.
- Focus on the state budget (other public budgets were not solved).
- Tendency to have well-balanced state budget, however, it is not possible in the first years of independent Czechoslovakia.
- Tendency to have state budget harmonised with practice.
- Partial allocation of expenditures and revenue of state budget.
- Different rules for parts of the territory (Slovakia and Carpathian Ruthenia).

3.2 1926–1929

The reform of public finance was realised through two key rules. The first one was Act No. 121/1926 Coll., on the state budget in 1927. This state budget was divided into four sections (state budgets involves revenue and expenditures of the activities based on solidarity, business results of state companies based on market mechanism, other subjects of the public sector, e.g. municipalities, and management of state debt). Non-budget funds were added into the system of state budgets. These were important for investment activities lasting longer than one year (Pavel, 2003).

The second key rule was Act No. 76/1927 Coll., on taxes. It changed the structure and the construction of direct taxes. Karel Engliš (Minister of Finance) wanted to bring theoretical knowledge into praxis. Therefore, the tax system was divided into three parts. The first one was direct taxes (the most important), the second one was indirect taxes and the last one was

charges. The tax system was well-arranged, and it ensured uniform taxation in the whole country (including Slovakia and Carpathian Ruthenia).

The second period is characterised as follows:

- Separation of fiscal and monetary politics.
- Unification of all rules within the whole territory of Czechoslovakia.
- Well-balanced or surplus state budget.
- Stabilisation of public finance thanks to economic expansion (decreasing state debt originated in previous period).

3.3 1930–1938

The Great Depression had a negative impact on public finance. State revenues decreased, state expenditures increased (workfare and public works). State budgets were accepted as well-balanced, but they finished as deficits. The Ministry of Agriculture played the main role and wanted to increase state interventions. Many taken steps were characteristic for a centrally planned economy. There were a few loans (two internal and one foreign) for infrastructure projects.

After the Great Depression in 1934 and later, public finance was not stable because it increased military expenditures. The Ministry of Finance wanted a restrictive fiscal policy, but the Ministry of National Defence needed more money. In 1937, military expenditures represented more than 37 % of state expenditures. In these days, tax rates increased, and new taxes were established (tax of state defence or special profit tax, see Act No. 247/1937).

Czechoslovakia emitted state obligations and tried to gain money through long-lasting loans. However, capital market in Czechoslovakia was limited and gaining foreign loans was improbable, so the Ministry of Finance adopted new regulation – banks had bought state obligations. (Pavel, 2004). These steps were not enough; the Ministry of National Defence needed more money. For this reason, the Ministry of Finance and the National Bank of Czechoslovakia started a monetary expansion. The National Bank of Czechoslovakia increased the number of small money.

The third period is characterised as follows:

- Increasing of state debt and stopping of state obligation redemption.

- State revenue increasing (especially increasing tax rates and establishing new taxes) and state expenditures (loans, state obligations) for arms programme.
- Mandatory buying of state budgets by bank sectors.
- Interconnection of fiscal and monetary politics for increasing money for arms programme.
- Only possibilities how to increase revenue were examined, developing of theory and needs of municipalities were inhibited.

3.4 1939–1945

According to History of the Ministry of Finance of the Czech Republic, the relationship toward public finance was one-sided during World War II – increasing the public deficit. In 1939, the planned deficit was 7 billion CZK. Czechoslovakia lost one-third of its territory due to the Munich Agreement, but the total state deficit was on the same level. The amortisation of internal state debt was interrupted; only interests were paid. At that time, revenue was increased through new taxes. Expenditures on defence were decreased. President and imperial protector accepted the state budget.

In 1940, the state budget was not created. In the following years, state budgets were created, and they were still deficient. The total war deficit was 20,3 billion CZK. In 1942, the amortisation of internal state debt began. Payments in relation to external debt were interrupted. In connection with losing one third of the territory and based on agreements with Germany, Hungary and the Slovak Republic, total state debt was decreased by 9 billion CZK.

There were many changes in tax rules. "*According to the introduction of the wartime economy order (Kriegswirtschaftsverordnung) in September 1939, all income tax increased by half. Newly, earnings higher than 2 400 RM were subjected to a tax. War surcharge (Kriegszuschlag) on the original tax was capped at a maximum of 15 % of income, while the upper limit of the actual tax rate could be up to 65 %. Taxation of individual income was highly progressive. Earnings between 1 500 and 3 000 RM a year were taxed with 20 % income tax rate (Einkommenssteuer, Lohnsteuer) in the early years of the war, income between 3 000–5 000 RM by 55 %. In the same order, corporate income tax (Körperschaftsteuer) was increased by 66 %.*" (see Johnson, 2017).

Many German tax rules were implemented (e. g. tax of return), new taxes were established (e.g. property tax, corporate tax, fire protection tax, taxes on the use of transportation and visits to cinemas and theatres). Taxes with a special character such as income tax and occupation payments or racist tax for Jews, Gypsies and Poles were introduced.

The fourth period is characterised as follows:

- Increasing of tax revenue (especially tax rates and establishing new taxes for its coordination with Germany).
- Decrease expenditures for defence.
- Increasing of indebtedness and devastation of public finance.

3.5 1945–1989

First years after World War II, the government decided to gain money from loans. The state budget in 1946 was divided into two parts; one part for the Czech Republic and one part for the Slovak Republic. The state budget was regular and irregular while the budget deficit this year created more than 26 billion CZK, see Act No. 160/1945 Coll.

The main change was the level of nationalisation. All companies were transformed into national companies. They were managed separately from the state budget, but they were obliged to send one-half of profit to the state budget in the first years after nationalisation. During the totality, all state budgets were planned as well-balanced. However, this well-balance was reached artificially in cooperation with the State Bank of Czechoslovakia through state obligations.

The economy of socialism showed these characteristics – prohibition of private business, foreign and internal trade monopoly, regulation of prices and collectivisation. Taxes were adapted to socialist economy – agriculture tax, tax from literary and art activities, sales tax etc. In 1964, car tax was added into the tax system and personal income was taxed differently with respect to the type of property or merit of personal income (see History of the Ministry of Finance of the Czech Republic).

The fifth period is characterised as follows:

- Interconnection of fiscal and monetary politics (due to the funding of state debt through emissions of state obligations).
- Well-balanced state budget (but it was only a game to play with numbers).
- Central planned economy with establishing socialist economy taxes and harmonisation with the Soviet Union.
- Devastation of public finance; the theory of public finance was regulated according to the needs of a socialist state.

3.6 1989–till now

The new politic situation caused economic transformation and brought many changes to the theory of public finance and its implementation. Czechoslovakia and then the Czech Republic tried to follow the situation before socialism. In 1993, a new tax system was established (it introduced new taxes like import tax, or cancelled others like sales tax). The new tax system should have helped business and increased tax fairness. However, not all steps had a positive impact on the overall economy.

The base of the tax system is valid until today. Many changes were necessary especially in the area of indirect taxes. In 2003, consumer taxes were changed. In 2004, value-added-tax was newly established. It was necessary to implement it before our entry to the EU.

State budget takes first place from all public budgets. It was well-balanced in the first years after transformation. In the last twenty years, state budgets are drafted as deficits and our state debt has increased during this period. Public revenue is still increasing but public expenditures increased more quickly. There were only two years with a surplus of state budget (in 2016 and 2018), the reasons were economic expansion and income from the EU (the Czech Republic receives more money from the EU than how much has to pay).

The last period is characterised as follows:

- Separation of fiscal and monetary politics.
- State debt increased (from 0 % to 34 %).

- Come back of the Czech Republic to the market economy and harmonisation of public finance with EU rules.
- Theory of public finance differs from the practice (state debts during economic decrease and economic expansion as well).
- Aiming at the state budget and low attention to the rest of public budgets (they are often well-balanced), more restrictions relate to municipality budgets (e.g. Act No. 23/2017 Coll., on the rules of budgetary responsibility).
- Missing politic responsibility for public budgets.

To sum up, reality shows that approaches to public finance have been changing during the one-hundred-year period based on the political situation. There were periods when fiscal and monetary policy were separate and periods when fiscal and monetary policy were interconnected. In the first years, the major part of public finance was spent on investments. The current situation is contrary – most public expenditures are spent on redistribution. Unfortunately, public finance often finished in deficit and had a bad influence on economic development. Last period shows that this tendency does not change which could cause a big problem in the future.

4 Conclusion

If we ask a question of how to define current public finance, then based on the above-mentioned economic and legal considerations, it is possible to conclude that:

- Public finance is a comprehensive category for social relations sui generis which are part of monetary relations.
- The object of public finance is public money.
- The content of public finance is formed by the monetary transactions through which public money funds are realised, distributed, and the rights, authorisations and obligations associated with it.
- Public finance is always implemented in connection with the public sector.
- The existence of public finance is assigned primarily to the satisfaction of the public interest (Mrkývka et al., 2014).

It is obvious that the virtual and reality conception should be the same, however, it is possible to notice some differences. The practice shows that it is lagging the theory (which applies especially for politics). Theory shows what public finance should solve, but current politics use public finance for its own purposes and needs. For this reason, we confirm the hypothesis that virtual and reality conception of public finance differ. The partial hypothesis was confirmed as well; economic view on public finance is more detailed than enactment.

Finally, the issue of public finance and the public sector is and will continue to be at the forefront of theory and practice. The theory of public finance must constantly address several issues, responding to emerging problems both on the national and international scene. It is also necessary to continue to emphasise the control of public finance in terms of economy, efficiency, effectiveness and transparency.

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Public Sector in European Union as Intelligent Customer and Efficient Public Procurement

Anna Wójtowicz-Dawid[1]

Abstract

Operation of public finance units, the tasks implemented, and actions taken aimed at constant improvement should be a clear manifestation of their efficient functioning. Currently, the functioning of public finance units in the European Union is not effective. Spending public funds, or more precisely expectations regarding the methods of spending public funds, have changed significantly over the last couple of years. Among others, this can be clearly seen in the direction in which provisions regulating public procurement change in the European Union. Price is no longer the basic criterion when procuring supplies, goods or construction works as other values gain in importance. Effective spending of public funds becomes a tool for achievement of an increase in quality, innovativeness, usability or environment protection. The main goal behind this paper is to discuss efficient public procurement from the perspective of such features, tools and obligations of an ordering party who is assigned the properties of an intelligent customer. Research methodology mostly includes law tools i.e. mostly legal doctrine and to a limited extent comparative law methods. Additionally, to verify correctness of my hypotheses I use analysis rulings of the Court of Justice of the European Union. As a basis for this analysis I assume that actions taken by an intelligent ordering party allow for achieving efficient public procurement.

Keywords: Law; Public Procurement; Intelligent Ordering Party; Spending Public Funds; Efficiency.

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1 Introduction

When purchasing goods, services or construction works a public finance unit becomes a customer of its contractors. Service providers, sellers or companies providing construction services are aware of what a customer means for their operation on the market. Therefore, it is greatly important for them to recognize and classify customers as it increases the efficiency of their sales activities. On the other hand, awareness of the customer, his/her needs and expectations is crucial for correct customer analysis.

Purchases of goods, services and construction works differ a lot in terms of their preferences and development perspectives. A. Stachowicz-Stanusch and M. Stanusch rightly point that for every entrepreneur it makes no sense to invest in customers with low potential or low generated value. In the same way, it makes little sense to spend significant resources on those who have long been loyal customers as they will no leave for another supplier or service provider (Stachowicz-Stanusch, Stanusch, 2007: 34). Correct customer segmentation is crucial for an enterprise and it becomes a method for analysis the nature of customers' needs, perception of their expectation by assigning them to a specific group of entities and people with similar needs, perception or expectations as well as requirements (Horovitz, 2006: 26).

Public procurer is a special customer, who, when placing its order, makes its choice dependent on regulations included in public procurement system.

European public procurement market has been recently undergoing a series of well-visible changes. These are caused by a need to reconstruct the public procurement system that should not only be directed towards meeting the needs of public administration, but it should also take into account the role it plays in meeting citizens' needs.

Public procurement becomes a tool for instilling citizens' trust in public administration bodies. With this assumption in mind, public finance units shape their policy in selected social or economic areas with the use of public procurement. The ordering party thus becomes a special customer. By making an informed choice, it models, among others, its needs and expectations at the same time influencing specific social life areas, business trading, which in turn allows for development of specific industries or economic sectors

that would not have stood any chances for development or existence otherwise. As F. Fukuyama rightly points, public procurement is a necessary precondition for economic development in such cases (Fukuyama, 1997).

The main goal behind this paper is to discuss efficient public procurement in Poland from the perspective of such features, tools and obligations of an ordering party who is assigned the properties of an intelligent customer.

Research methodology mostly includes law tools i.e. mostly legal doctrine and to a limited extent comparative law methods. Additionally, to verify correctness of my hypotheses I use analysis rulings of the Court of Justice of the European Union.

As a basis for this analysis I assume that actions taken by an intelligent ordering party allow for achieving efficient public procurement.

2 Efficiency

The scope of financial law increases with the higher financial activities of the public sector and with the higher number of state intervention into economy. (Janovec, 2017)

Increasing the effectiveness, efficiency, and compliance of public procurement has become an ongoing concern for governments. Public administrations at different levels are realising that – in order for PP to fulfil its mission – appropriate control and diagnostic systems must be put in place. (Patrucco; Luzzini; Ronchi, 2016)

To be able to correctly determine the conceptual range of efficient public procurement, the notion of efficiency needs to be defined first.

When speaking of efficient public procurement we should mostly have economic efficiency in mind. Efficiency is not a notion whose scope results directly from public procurement regulations. However, it is a tool used in public administration, to be more precise in assessing effectiveness or efficacy of administrative operations.

G. Kozuń-Cieślak points that "*in modern world the category of efficiency has gained the status of an imperative at any economic level (micro, mezzo, macro) and in each business sector (private, public, non-profit)*" (Wicierzyńska, 2016: 559).

According to W. Gasparcki efficiency should be understood as economic action taken efficiently i.e. effectively and economically (Puszka, 2015: 15).

Effectiveness may be identified with smooth, good job broadly discussed by T. Kotarbiński (Kotarbiński, 1958: 395).

In the doctrine it is often pointed that all the changes in selected area of operation of public administration should contribute to smooth and economic operation of state authorities and strengthen the rule of law in their operation, increase social participation, improve administration culture, shorten service time by doing tasks more efficiently, and finally achieving maximum effect with minimum costs (Jełowicki, 1969: 10).

Government efficiency is understood as the capacity (potential) of state authorities and administration (at various management levels) to implement public policies in an efficient, just and economic manner (including adjusting the scope of public intervention to actual social needs). Among others, this relates to providing basic social services, increasing citizens' life level, eradicating poverty and ensuring economic development. Shaping appropriate qualifications and human resources in public sector, appropriate regulatory competences as well as honest administration and counteracting corruption become crucial efficiency constituents (Rutkowski, 2009: 68).

J. Zieleniewski points to the facts that recipients of public administration services include citizens requiring appropriate standard of the services provided. Thus the goal may be defined as providing administrative service or high quality or "aiming at high satisfaction levels among external customers", and the level of achievement can be measured with general measures: "satisfaction of external customer on service in the office" as well as with standards measuring specific attributes of services provided by the office (e.g. access to information, employee competences, service time etc.). Therefore, it perceives effectiveness as achievement of the goal set (Zielenieski, 1975: 230).

In economic literature there is a difference between efficiency and effectiveness, the latter being understood as degree of goal implementation and the former being understood as optimization in the ratio between outlays and results.

P. Modzelewski, when discussing effectiveness in public administration, points to administrative services for which it is assumed that effectiveness connected with specific attributes in public service will be defined as "relative effectiveness". Terminological distinction of "relative effectiveness" allows for directing attention to specific criteria for assessment and more detailed, extensive analysis (Modzelewski, 2007: 70–71).

As A. Pyszka points, analysis of hypotheses presented in legal doctrine shows that efficiency covers a wider scope of notions with which it is identified, among others effectiveness, proficiency, performance, productivity. At the same time, efficiency relates to result without limiting itself to a specific indicator, but to some state/feature of being efficient. This leads to another take on efficiency, which translates into various perspectives from which is should be analysed (Pyszka, 2015: 2). Efficiency in the narrow context is identified with economy and in the wider context with effectiveness, profitability and economy. It is also sometimes identified with performance and productivity. For economists this means results of the whole organization or unit divided by resources used to generate them, with both results and resources expressed in financial value (Pyszka, 2015: 15).

The essence of effectiveness is also presented in legal doctrine in behavioural meaning as the goals of the organization and the individual are perfectly integrated. This points to potentially high level of efficiency as the individual would do his or her best to achieve organization goals (Nowosielski, 2008: 6). As Kotarbiński stresses when analysis efficiency in its social context, the results go beyond economic issues (Kotarbiński 1971: 79). This allows for a different take on efficiency, including viewing it as adding transformation social attitudes, humanization of human relation and moral sublimation (Sokołowski, 1971: 23). As an effect of such an outlook, efficiency is not only interpreted from the perspective of effectiveness but value and degree of preferences. Perception of efficiency in extra-financial sense covers the social dimension, relations with the environment, what definitely goes beyond perceiving efficiency from the economic perspective, where profitability, service costs of public financing levels count.

Efficiency also takes into account practical issues, relating to administrative resources and professional skills of the staff responsible for public procurement (Pauw, Wolvaardt, 2009: 76).

Testing efficiency in public finance sectors is possible mostly within the scope of analysing cost efficiency as these are not organizations geared towards maximizing profits, thus it is not possible to analyse profit efficiency.

3 Efficiency and frugality rule in spending public funds

Frugality belongs to criteria that assess disposing of financial and material resources from the perspective of achieving specific goals. B. Kuc shows that American literature in management stresses productivity as economic measure of efficiency (Kuc, 2008: 87).

According to J. Miodek, a frugal person can be "defined as somebody who can, in a good and sparing way, manage what she or he has or was entrusted with, and who, when managing money, uses it right to achieve the defined goal." Frugality is the "ability to manage and administer something well", it's "skilful and frugal management" (historical dictionaries stress evolution of these words towards their economic meaning). The criterion (measure, test, benchmark) of frugality should thus be understood as "*a set of factors on the basis of which we assess whether something entrusted for use is managed in a good and frugal manner, whether a given activity is managed skilfully and whether financial resources intended for implementation of a given undertaking are used in a rational manner*" (Miodek, 2002: 5–6).

L. Kurowski stresses that when observing legal doctrine's position on the criterion of frugality, it needs to be pointed that it evolves significantly from assessment of thriftiness, cost efficiency to frugality. However, it is always useful that the controller has knowledge on economic analysis, analysing stock, fixed assets, profitability etc. (Kurowski, 1968: 58).

A. Kubik points that frugality covers analysis of fund spending efficiency. The criterion in question analyses optimal use of financial and material resources and optimization of organizational measures taken (Kubik, 2004: 167–169).

According to O. Lange, maximum strive at a goal used to be at the heart of frugality, but in such a manner as to achieve maximum goal implementation with given outlays or as to achieve minimum time expenditure. (Lange, 1967: 217–218)

Apart from the criteria mentioned above, transparency and openness are often cited. A. Kubik defines them as determining responsibility of the people disposing of public funds, noticing instances of uneconomical management, limiting the risk of public funds being spent in inexpedient manner with simultaneous free access to data connected with public funds and methods of managing them (Lange, 1967: 217–218).

Audit standards of the Supreme Audit Office point that "*frugality covers analysis of: economic and efficient use of resources, achieving appropriate relations between expenditures and effects (results of activities in conditions in which the audited unit operated and whether it was possible to achieve it with lower expenditures or whether it was possible to achieve a better result with the same funds); using the possibilities of preventing or limiting damage*" (NIK, 2002: 8).

4 Efficient public procurement

The main goal that the European Union has set for coordination of public procurement procedures was to minimize risk that ordering institutions would use premises other than the economic ones when granting public procurement (Court of Justice of the European Union, C-380/09). Bid selection should be based on criteria for assessment of the economically optimal bid, which does not mean that this needs to be the cheapest one. This also confirms the hypothesis that purely economic grounds should be at the basis for granting any public procurement for any ordering party. Economic situation of the ordering party is understood as its resources or reasonably defined needs to which the description of the object of procurement or bid assessment criteria points.

The Court of Justice of the European Union (hereinafter CJEU) in its ruling of 17 September 2002 in case C-513/99 pointed that in line with directives relating to public procurement, in a situation when bid is granted on the basis of the criterion of economically optimal bid, the ordering party may take into account various factors connected with the procurement, such as for example: quality, technical advantages, delivery deadline, duration of implementation or price. Not all the criteria for bid selection need to be of purely economic character. Then, it its ruling of 4 December 2003 C-448-01, the CJEU

pointed that not only does the ordering institution enjoy freedom in establishing bid assessment criteria, but it also enjoys freedom in determining their weight, on condition that the weight assigned to specific criteria aim at selecting the best offer in the light of the accepted criteria.

T. Kocowski thus rightly assumes that spending public funds intended for performance of public services should be done in efficient manner. He also points that public procurement is about available resources guaranteeing maximum and optimal performance of public services, by guaranteeing the largest amount of the desired and by allowing the largest possible scope of necessary services (Kocowski, 2012: 23–24).

Efficient public procurement is a procurement granted in line with the provisions of law in force. Within this meaning, efficiency is connected with lawfulness of the public procurement procedure. Spending public funds should be perceived through regulations on public procurement, and not only on assessing lawfulness of the actions taken. What is crucial is the strive at achieving maximum level of satisfaction of goals, expectations and needs set by ordering party while minimizing the incurred costs at the same time. Here, again the perception of cost should not be limited to purchasing goods, services or construction works, but it should rather be geared towards verification of life cycle costs. Often, this aspect is completely left out and cost is only viewed through the prism of purchase price. Such an approach seems incorrect from the point of view of frugality in public funds spending.

Economically efficient procurement is one that guarantees the best possible ratio between expenditure and effect of implementing the procurement as a result of smooth, quick procure that is open to innovation. The element influencing efficiency when granting public procurement include: innovativeness, modern electronic solutions, ecological and social criteria. Then, it is crucial to develop such terms of reference that would leave a lot of freedom to the contractors in providing innovative solutions. On the part of the ordering party this enforces precise definition of expectations and goals that the procurement should bring about with simultaneous determination of the expected values of results described.

Among the basic rules for efficient public procurement, the World Bank mentions the economy rule and the effectiveness rule understood as the efficiency rule. Public procurement is viewed as a process whose main goal is to guarantee the ordering party that procurements are granted according to the *best value for Money* principle (The World Bank, 2003). In turn, the World Bank understands efficient public procurement as procurement that is granted fast, without unnecessary problems and delays.

Efficient activities and creating value at lower costs is important from the point of view of the Value for Money concept (Niven, 2002: 299).

Public procurement largely has strategic aspirations, and its potential to deliver on wider societal issues is attractive to policy makers. Public procurement often lacks strategic maturity and critical issues, notably around how to demonstrate and evaluate its impact and "success". (Grandia, Meehan, 2017)

5 Factors weakening efficiency in public procurement

According to E. Ruśkowski streamlining public spending constitutes a precondition for dynamic and harmonious development of Poland. He also presents a hypothesis according to which the structure of income source of local government units prioritized adjusting funds to the scope of implemented tasks (Ruśkowski, 2005: 120–124).

When analysing procedures based on public procurement regulations, attention should be paid to a series of factors that influence lowering efficiency in spending public funds.

The biggest limitation in public procurement efficiency includes lack of professionalism on the part of the ordering party and the contractors. Usually, ordering parties base the description of the object of procurement on what they have worked out in many years. They do not strive to change their approach to descriptions fearing innovative solutions. The fear of novelty mostly includes resistance against totally new, previously untested, technologies.

Efficient procurement processes require efficient communication between the engaged units (ordering staff, financial planners and decision makers)

as to contribute to identification of needs, timely assessment of budgetary availability and future reasonable planning. Failure to communicate effectively results in failure to identify needs.

Communication needs to take place both within the ordering institution, guaranteeing active participation of all the internal key stakeholders, such as technical experts, designers, or lawyers, throughout the whole procurement procedure. This would allow for clear determination of needs and technical requirements, and it will also stimulate effective implementation. It is also necessary that various ordering institutions communicate i.e. that there is cooperation between ordering institution at regional, national and European levels which is especially of an advantage in case or scarcity of resources for technologically demanding tasks and for identification of common needs (sharing risks).

Indispensable element of all the public procurement procedures includes market analysis to determine the needs that should be satisfied and then drafting terms of reference. Lack of knowledge on goods, services, methods for satisfying customers' needs by contractors with the offered products constitute one of the barriers in efficient public procurement. The ordering party has no or only minimal knowledge that would allow it to describe the object of procurement is a way allowing to getting bids offering maximum satisfaction of ordering party's needs while at the same time minimizing costs connected with procuring it. Directive 2014/24/EU, in preamble 73 points, that new strategies for cooperation in public procurement may allow for ordering institutions to "make maximum profits out of the internal market potential by using the effects of scale and sharing risks and benefits".

Without any doubt the factor negatively influencing development of efficient public procurement are audit activities taken by competent audit authorities. They mostly examine lawfulness of ordering party's actions. As P. Szustakiewicz rightly points the audited bodies behave in overcautious manner taking such actions that do not make them at risk of accusations on the part of auditing bodies: "*we are dealing with a kind of Italian strike in administration, as it takes such actions as to strictly observe the procedures. It does not engage in any innovative actions that would streamline their operation. In such a situation, observing procedures becomes a goal in itself (.)*" (Szustakiewicz, 2013: 42).

Apart from the factors mentioned above, political environment in which public procurement is granted also plays a role. Groups of interests, lobbyists, politicians interested in creating specific model of public procurement system or even in specific tender results form a barrier preventing development of efficient public procurements (Thai, 2009: 7).

6 Public sector as intelligent customer

Intelligent ordering party in the public procurement system is a customer that skilfully uses instruments included in regulations shaping the public procurement system to guarantee efficiency of the public procurements granted. This requires both theoretical and practical knowledge on public procurement, which translates into awareness of both competences and limitations within this scope.

Awareness of available resources, precise determination of needs that public sector wishes to satisfy with a given procurement and, what follows, knowledge of the market of goods, services and constructions works offering the latest technical and technological solutions within its reach are indispensable attributes of an intelligent customer. We might conclude that an intelligent customer is aware of available resources and its own expectations in relation to final effects of the procurements granted. At the same time it has skills for adjusting its expectations to the resources within its reach. It avoid purchasing solutions that satisfy its needs only partially or even not at all.

Economic theory of rational choice (Cooter, Ulen, 2011: 25–34), implemented for the needs of economic analysis of public procurement law shows that before making a decision on commencing public procurement procedure each ordering party engages in detailed analysis of costs and advantages connected with the procedure to maximize profits from the procurement granted. Analysis of costs should not only consist in verifying purchase costs. It is necessary to run product or service life cycle costs analysis, as viewing costs in specific time perspective would allow for actual assessment of cost effectiveness of a given procurement. In legal doctrine it is often stressed that ordering parties' decisions often escape schemes of rational choice theories (Thai, 2009: 5–6).

Intelligent ordering party is also characterized by the so-called right market intelligence. Getting to know the market characteristic for the object of procurement, it checks what technologies and products constitute innovations that it could use. Market analysis allow for verification relating to the number of contractors and potential necessary for implementation of a given public procurement, which is crucial not only for the performance of the object of procurement, but also for selection of appropriate procurement granting mode (European Commission, 2010: 94).

A public finance unit may verify the assumptions made for a given public procurement as get knowledge on market possibilities, offered products or possibilities of creating a given product, service or construction work by running the so-called market research. The public unit invites potential contractors and financial institutions for participation if implementing the investment in public-private partnership mode, presenting the stakeholders with the so-called information memorandum. It is a document describing the initial scope of financial, legal and technical assumptions for the planned investment. The array of issues subject to market research is only limited by needs of the public entity. Such market consultations allow the ordering party to determine solutions offered by the contractors, the range of ordering party's needs that they are capable of satisfying and costs that it needs to bear in connection with it.

Professionalism of the procedure conducted on the basis of public procurement also includes care of correct and rational spending public funds. In practice, it can be observed that public sector tries to make savings on professional services. Lack of professional experts in specific branches of the economy, with knowledge on the latest technologies or products entails the risk of negative influence on efficiency of the procurements granted.

European Union made the vision, new priorities and development goals more precise in basic strategic documents entitled "Communication from the Commission, EUROPE 2020, A strategy for smart, sustainable and inclusive growth" (European Commission, 2010). This Strategy stresses on several occasions that it is necessary, both at the level of EU, member states and regions, to make intelligent, wise choices, called intelligent specializations.

Public purchasers, in order to act as intelligent customers who plan what they will need to purchase (the need for innovation), need to precisely define how to procure it on time and how to organize the process by openly communicating to the market their long-term plan to give all the existing and potential suppliers (contractors) time to react and create solutions responding to the defined needs.

7 Conclusion

The public procurement market in European Union is about constant clashes of interests. On one hand there is interest of the ordering party aiming to get the most economically favourable procurement, on the other hand there is interest of the contractor wishing to sell its goods and services. The ordering party's position dominates, as it is the ordering party who shapes description of the object of procurement, bid assessment criteria thus having significant influence on shaping rules for selecting a contractor. It is thus necessary to make the ordering parties aware that the existing public procurement system allows for the existence of intelligent ordering party.

Public finance units, to be treated as intelligent ordering party, need to efficiently use solutions included in the public procurement system while at the same time remaining aware of their needs, market opportunities paying attention to full professionalism of those running the procedure.

By taking actions aiming at commencing public procurement procedure, it is necessary to make a description of the object of procurement, precisely determine all the needs that the procurement can satisfy. The market analysis performed later would allow for verification of opportunities that transaction partner may offer while simultaneously analysing cost efficiency of the offered solutions. The cost efficiency should both be limited to getting the purchase price. It needs to cover comprehensive costs of acquiring, using and waste management i.e. all the life-cycle costs. Necessary element from the point of view of public procurement efficiency includes intelligent ordering party using analysis of costs and benefits. It allows for selecting the bid with the lowest cost over the whole period of operation. This is because purchasing optimization lies in ordering party making informed decisions.

By drafting the description of the object of procurement, the ordering party should take into account all the elements that could influence cost born over the whole period of using the object of procurement. When shaping bid assessment criteria, it should formulate them in such a way as to assign correct weight to criteria influencing efficiency of the procurement.

The policy of efficient public procurement in force in the European Union forces the ordering parties to change their policies and plan implementation of public procurement. It inclines them to grant public procurement with the greatest added value i.e. meeting specific social or environmental goals. This entails that the ordering party must bear the characteristics of an intelligent ordering party.

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PART 2:
TAX LAW

TAX LAW – LEGISLATION AND GENERAL ISSUES

Law as a Tool to Combat Tax Evasion[1]

Mária Bujňáková[2]

Abstract

The author of the paper deals with one of the EU priority policies, i.e. tax policy and within its scope the fight against tax evasion and avoiding tax duties in the sphere of both direct and indirect taxation. It highlights assorted measures taken by the EU and those at the national level. The author also emphasizes that even the terminology used in this sphere shows that certain level of avoiding tax duties is tolerated, or even expected.

Keywords: EU; Taxes; Tax Policy; Tax Evasion.

JEL Classification: K34.

1 Introduction

Tax policy is part of the State budgetary policy and, at the same time it is also an instrument of the State economic policy. We may say that it is actually a set of measures by which the State modifies the tax system. Tax policy has its objectives, both economic, political and social, and, above all, the tax system of the State is used as a means of achieving them. In particular, tax policy should be stimulating, which promotes economic development as well as entrepreneurial activity. When applying tax policy, however, it is necessary to take into account the specifics of the State and therefore it is not possible to fully apply the tax policy of another State to our conditions. Each country has its own specifics, a degree of development, a social structure,

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a geographical location, and many other features and specifics, which must also be respected in fiscal policy.

The tax policy is a very broad and complex issue. Taxation in every market economy is an often discussed professional issue, but also one of the most frequently asked questions by the public. In order to achieve the prosperity of the country, the rational economic policy of the State and pragmatic financial policy are necessary. If a State wants to focus its economic policy on a particular area of interest, it can do so through targeted policies that form its part. To achieve these goals, the law also serves as a tool for regulating socioeconomic relations. It should be noted that law is generally not very positively perceived, although sometimes it is only a one-sided view, a statement. On the other hand, there must be certain types of management that the company can provide for the individual needs. In addition to other instruments, law is a tool that should be the guarantor of the required creation, the anticipated development, but also the termination of any social relationship guaranteed by the legal norm.

The legal system is a regulatory system sui generis (Krecht, 2002: 584). Regulatory tools are mainly legal norms. Legal norms are generally perceived as objectively-bound general binding rules of conduct, expressed in State-determined or recognized form, the observance of which is enforceable by the State authority (Brôstl; Kanárik; Dobrovičová, 2004: 68).

Law as a phenomenon is inherently inseparable from the society in which it arises and operates. In addition to this conditionality of law, the social context of its existence can also identify the conditionality of the development of social relations by a valid and effective set of legal norms that are implemented in it. It should be added that tax law as a special group of legal norms is inseparably linked to the State, but the economy has a decisive influence on the standard of living of the population.

The authority to levy the taxes is one of the fundamental attributes of sovereignty of EU Member States. Attempts to achieve tax harmonization in the current period are not at all realistic, although there exists a considerable interest in political expressions, debates, but it is always at the level of expressions, and the reality is obviously unattainable for a number of reasons, notably economic but also political ones (Červená, 2013: 49–66).

The EU Member States have transferred only limited powers in the area of tax policy and legislation. The original EU taxation measures have been focused on the smooth functioning of the internal market, with the focus only on indirect taxes. In the field of direct taxation, discussions and efforts to harmonize these taxes are more and more resonant in recent times, even though it has to be said that they are still unsuccessful (Kicová, 2011: 114–121; Romanová, 2012: 522–533). It is true that the EU is stepping up the fight against tax evasion and avoidance, as these pose a threat to fair competition and cause a significant drop in tax revenue. On the other hand, it should be noted that the tax measures adopted in the EU must be adopted by the Member States unanimously. Tax policy itself is largely influenced by the jurisprudence of the European Court of Justice, with the European Parliament having only the right to be consulted in this area, except for budgetary issues where the Council, as a component of the budgetary authority, shares decision-making powers with the Council.[3].

2 Objectives and Solutions to the Tax Issues set by the EU and their legal basis

The EU Tax Policy Strategy is stated in the Commission Communication on Tax Policy in the EU – priorities for the coming years (Communication from the Commission to the Council, the European Parliament and the Economic and Social Committee Tax policy in the European Union – Priorities for the years ahead). Provided the Member States comply with EU rules, each of them can freely choose the tax system they deem most appropriate. In these frameworks, the main priorities were declared to eliminate tax obstacles to cross-border economic activity, to combat harmful tax competition, and to promote greater cooperation between tax administrations in controlling and combating fraud. Greater coordination of tax policy would ensure that Member States tax policies support broader EU targets than those set out in the Europe 2020 Strategy for smart, sustainable and inclusive growth.

3 Information sheets on the European Union are available at: http://www.europarl.europa.eu/at yourservice/sk/displayFtu.html

The legal basis for tax issues in the EU is the Treaty on the Functioning of the European Union, the chapter on tax provisions (Articles 110–113) on the harmonization of legislation. The development of the EU tax provisions is primarily focused on the smooth functioning of the internal market, while it should be emphasized that indirect tax harmonization was addressed earlier and to a greater extent than direct taxation, although it has to be emphasized that individual trading practices often lead to abuse and evasion by individual subjects of law.

Tax reports published by the Commission highlight the EU tax outcomes but also issues that still need to be addressed. The very frequent issues raised by the Commission include direct and indirect taxation, tax evasion and tax avoidance, State aid decisions and regulatory infringements.[4]

One of the most important and most fundamental issues of EU tax policy is, above all, the fight against tax evasion and tax avoidance. The issue of tax evasion has become one of the Commission's most important issues and priorities. The fight against tax fraud and evasion involves direct taxation (in particular measures to combat harmful tax practices) and indirect taxation (unpaid VAT). Annual tax revenue losses in the EU as a result of tax evasion and avoidance are, according to the calculations, a considerable amount in euros, which means a large loss of government revenue but also a threat to fair competition.[5] In May 2013, the Council adopted conclusions on tax evasion and tax fraud, highlighting the need to combine efforts at national, EU and global levels, but also endorsed the support of the G8, G20 and OECD work on the automatic exchange of information. Gradually, these measures are being put into practice, although it should be noted that their application in practice, but especially their administrative implementation and cooperation, is a relatively complex and long-term process. The role of the European Parliament in this area is rather difficult. Although the European Parliament has generally supported the basic direction of the Commission's taxation programmes, the parliamentary vote is the biggest problem, even though there has been an attempt to move to a qualified

4 See also: European Commission. Available at: https://ec.europa.eu/commission/index_en

5 These issues were the topic of Commission President Juncker's letter to the Council and the Parliament Presidents.

majority vote on some aspects of taxation. The EU Parliament adopted a resolution focusing on the three priority areas of EU tax policy:

- Enhancing the benefits of the internal market through tax policy.
- Combating tax fraud, tax evasion, aggressive tax planning and tax havens.
- Implementing the enforceable tax coordination to ensure a long-term growth-oriented economic policy.

The fight against tax evasion and tax fraud is one of the Commission main priorities. The Commission has presented a package of tax transparency measures, which is seen as the basis for combating tax evasion. Tax measures are an area of the Union policy where we are quite clear about what a good association of countries in the EU really is. Against the circumvention of tax payments in particular by large multinational companies, the Union countries can only fight together. However, the EU countries are fighting two fronts. They also struggle with tax evasion at home, so it is also necessary to create a legal environment within the national legislation to make the legislation clear and to penalize those tax evaders and tax fraudsters, but at the same time there is a legal sanction to eliminate tax evasion and fraud.

3 Tax evasion and its definition

As tax evasion is marked situation where the taxpayer either partially or totally avoids paying the tax. We can say that this is a very simplified definition of tax evasion. The definition of tax evasion can be seen from the economic point of view, but the legal aspect of the definition of tax evasion is probably also very interesting. The very term legal and illegal tax evasion evokes the fact that the tax system has considerable reserves. The Slovak tax system, with its application in practice, also points to the shortcomings that characterize these concepts.

It's probably the old saying applicable here that taxes are what guides us from birth to grave. Each State should have a tax legislation that is effective and efficient. Under these terms, the whole set of measures and options that make up tax legislation is hidden. The financial monolingual dictionary describes tax evasion as the tax entity's attempt to reduce (curtail) or evade

tax liability, either completely or in part. This may be a legal tax evasion that allows for ambiguities, inaccuracies or inconsistent tax laws, or non-sequential laws such as, for example, on accounting, customs law, foreign exchange law, and so on. Tax evasion occurs most often when unjustified use of tax relief, tax exemption, misuse of some depreciation methods, valuation of depreciation of tax arrears and other, the so-called legislative and tax-technical factors. In the sources, the so-called illicit tax evasion is described, which occurs by pretending or concealing circumstances that can reduce the tax burden or lead to tax evasion. In this context, the costs associated with tax evasion, the probability of its detection, the financial penalty for detection and the impact of the evasion on public revenue are monitored. Illegal tax evasion is linked to non-compliance with tax laws. Most often, the existence of tax evasion is justified by citizens' attitudes towards compliance with the law, the level of legal awareness, general tax morality, the transfer of some tax activities abroad, the possibility of using the tax hiding and also various socio-political, economic, social and international factors (Jankovská et. al., 2012).

Tax evasion can be characterized as a result of the economic behaviour of taxpayers oriented towards reduction or minimizing the tax burden toward the State. Modern economics textbooks consider a rather non-standard economy to be an optimal environment for tax evasion than a standard economy. It is dominant in poor countries and countries with a transforming economy. Especially in the transforming economies, the growth of illegal non-payment of taxes was mainly influenced by the following factors: the introduction of VAT with its demanding administrative requirements (Červená, Forraiová, 2016: 11–13), constant changes in tax laws, a lack of qualified staff ensuring tax accounting in accordance with tax laws, extensive bribery and corruption in tax and customs areas (Strelcová, 2006: 93–97). Illegal tax avoidance and the measure of avoidance results in tax evasion that damages public finance health. Generally, tax evasion can be characterized as a situation where the taxpayer partially or wholly avoids paying the tax.

It is often reported that there are legal and illegal tax evasions. Just such a breakthrough in legal and illegal law evokes in us that it is not possible

in the rule of law that the tax evasion itself be legal or illegal. When we think purely theoretically, the result of tax evasion is always the failure to pay part of the tax or the entire tax liability. The sources state that tax evasion can be legal in the form of a tax advantage or as a tax saving (Semerád, 2014). A tax advantage can ensure a taxpayer avoiding, for example, other tax rates. Tax savings include options that legislation anticipates, such as applying past losses, depreciation, deductible items, and so on. It follows from the above that these are tax losses as the purposes of legislation. Enabling law enforcement should be so clear and precise that we cannot talk about legal tax evasion. Illegal tax evasion is considered to be a situation where a taxpayer violates the law, that is, an unfair part of the income, overstates the costs or expenses, issues fictitious documents, includes non-taxable expenses. This is a situation where we can assume that the taxpayer's action is primarily aimed at lowering the tax, no tax, or enrich him/herself to the detriment of the State.

The underlying cause of tax evasion is the inconsistency between the State interest in levying as much tax as possible, and the taxpayer's interest one is in paying as little tax as possible. This mismatch could be at least partially offset when the State creates fair and effective conditions for citizens, and in the elimination of tax evasion, effective legislative measures should be taken but not only in one country, but these legislative measures should be topical even in a globalizing world economy.

From the economic theory of rational behaviour, it follows that every economic entity behaves not only in the field of taxation in a way as to minimize its costs or tax liability. There is no business entity willing to voluntarily pay higher rates if there are possibilities to minimize them, optimizations that can be implemented in a variety of ways. Most often it is a form of tax evasion, which often includes crime signs. There is even a debate about the fact that apart from tax legal and illegal evasion, there are other differentiations. It may be a deliberate, unintentional, temporary or permanent tax evasion.[6] These discussions clearly indicate the need to take real measures to prevent tax evasion.

6 For further reading on this topic I see: Dialógy o ekonomike a riadení. Vol. 3, 2001, no. 7.

The efficiency of the tax system of each State depends on the quality of the tax system, on a number of other economic and social aspects and on structural links, but it also depends radically and strongly on how society (State) looks at tax discipline, i.e. how it addresses the elimination of tax evasion – at an economically and socially acceptable level.

Tax evasion, especially of VAT, has become a cancer of the Slovak economy. On the one hand, they "tunnel-out" revenues from the State budget, on the other hand they greatly increase the burden on decent businesses and employees, who have to cover the budget hole through high taxes. The fight against tax evasion requires a robust, comprehensive and, above all, conceptual approach by all the State actors concerned and should be the responsibility of each responsible government. It is also one of the key means of consolidating public finances, which at the same time will help to establish a stable and transparent economic environment.

The effort of the Slovak legislation also resulted in measures to include criminal offenses in the Criminal Code. It has to be said that these institutions are gradually being introduced into life and when their real application shows how important it is to clarify the tax legislation. In this paper, we will not deal more closely with criminal liability, as it requires a much larger dimension and will be the subject of a further contribution to this issue.

The tax issue is very broad and complex. Taxes are within the market economy the most discussed financial concept among citizens and entrepreneurs in each company. Taxable entities around the world prefer a tax system that is simple, stable, understandable, with low tax rates and high-quality and fast tax services. These attributes should be the basis of each country's legislation. But in a globalizing economy, it has to be remarked that international cooperation in the field of taxation is an important fact. In general, tax evasion can be eliminated more effectively if a tax system that is predictable for legal certainty and stability is simplified and streamlined.

Simplifying and clarifying the tax system is just one way of preventing tax evasion (Červená, Hučková, 2015: 115–127). An important fact is the existence of tax havens that creates an environment for entities that have the opportunity to use tax havens and thus circumvent the obligation to pay the tax in question. In tax havens, foreign-owned firms are exceptionally

tax-advantaged, and although they have to respect certain conditions, it is always beneficial for them. Tax havens are mostly in the countries with a small area and a low population, but show high economic outputs. The number of the companies founded in some tax havens even exceeds that of the population.[7] The European Union should, in particular, seek to abolish tax havens that still exist in the EU, where companies have special regimes that are truly unacceptable. It is therefore necessary to introduce uniform standards in every area of the economy and to break down barriers between States, only to achieve the best effect from the common market.

When we talk about the elimination of some institutions outside of our legislation, it is worth mentioning some of the institutes that are in the competence of our legislation (Romanová, 2015: 181–189). It is not quite right to provide a variety of concessions for some firms and companies where, in an effort to reach the investor's arrival, different concessions are provided, which ultimately distorts the business environment. Tax reliefs are often used by business entities for a certain period of time, and then, after exhausting these concessions, business is transferred to another country. It is true that the existence of certain restrictions also exists in the case of tax concessions, but in the final analysis these distortions deform the business environment.

4 Conclusion

Tax evasion is becoming one of the important moments that is being given considerable attention. How Babčák (2017) mentioned, it is necessary to limit tax evasions, tax frauds and unjustified tax avoidance.

It should be noted that there has always been a certain percentage of business entities that have implemented tax evasion, as there are many ways to bypass tax authorities. The EU is also currently focusing on fighting these scams, but it is questionable how effective its methods will be. The Organization for Economic Co-operation and Development, as one of the important tasks, has also tackled the issues of tax fraud. In particular, all

7 The issue of tax haven is a global phenomenon. For more on this issue see also: https://peterstetka.wordpress.com /2014/02/18/danove-raje/

actors should tackle tax evasion, which is undoubtedly enormous and ultimately damaging public finance health.

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Tax Relief and Tax Planning – Remarks on the Law as it Stands and the Law as it Should Stand

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Abstract

Tax planning takes place when the means provided for by law grants certain rights to reduce taxation. This contribution deals with to analyse tax reliefs, as defined in the Tax Ordinance Act, in the tax planning process. The main aim of this paper is to confirm the hypothesis that not every form of tax relief within the meaning of Article 3 section 6 of the Tax Ordinance Act is a means which entitles the taxpayer to reduce, as part of tax planning, the tax burden levied on him. Analysis, synthesis and compare the available literature were method used for writing this paper.

Keywords: Tax Law; Tax Planning; Tax Relief; Tax Exemption; Tax Discount.

JEL Classification: K34.

1 Introduction

Tax planning is a legally acceptable method of reducing taxation. Tax law should eliminate aggressive tax planning. (Babčák, 2017). Generally, tax planning is a taxpayer's action or non-action, resulting in a reduction in the fiscal burden. Unlike tax avoidance, the tax advantage obtained as a result of tax planning does not contradict the object and purpose of tax law provision. It is quite widely accepted in the scholarly literature on the subject that tax planning is manifested in the taxpayer's use of means provided for in the tax legislation allowing the taxpayer to reduce the tax burden levied on him. This view is formulated both in the Polish (e.g. Gajewski, 2016: 107; Olesińska, 2016: 312; Koreń, 2014: 11; Macudziński, 2014: 40;

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Karwat, 2002: 16; Brzeziński,1996: 10) and foreign literatures (e.g. Frecknall-Hughes, 2018: 1–6; Quentin, 2017: 26–34; Calderon Carrero, 2016: 206–226; Alvarrenga,2013; Jacob, 2010: 808–825; Karimeri, 2011: 296–297; Merks, 2006: 272–281; OECD, 1987: 16; Wacker,1979: 13–20). Constitutional Court also expressed such an opinion (Constitutional Court: K 4/03). To be more specific, tax planning takes place when the means provided for by law grants certain rights to reduce taxation. It is commonly accepted in the literature that means to reduce tax burden that are accepted by the legislature include mainly tax relief and tax exemption[2]. In the Polish legal system, the norm defining tax relief is set out in Article 3 section 6 of the Act of 29 August 1997 – the Tax Ordinance Act. However, tax exemption, within the meaning of this definition, is a form of tax relief.

The aim of this paper is to analyse tax reliefs, as defined in the Tax Ordinance Act, in the tax planning process. It will be supplemented, given the limited volume of the article, with selected examples of tax reliefs governed in individual tax acts. This makes it possible to confirm a hypothesis that not every form of tax relief within the meaning of Article 3 section 6 of the Tax Ordinance Act is a means which entitles the taxpayer to reduce, as part of tax planning, the tax burden levied on him.

The subject-matter of this study was chosen due to the absence of literature which would contain a thorough analysis of the significance of tax relief, including tax exemptions, in the tax planning process. For this reason, the first object of research was the norm defining tax relief. Then, individual forms of tax reliefs were examined in the context of tax planning. These remarks were made using the basic research method in legal science i.e. analysis, supplemented by synthesis and compare the available literature on the subject.

2 Juridical concept of tax relief and tax planning

According to the norm contained in Article 3 section 6 of the Tax Ordinance Act, tax reliefs include tax exemptions, deductions, abatements or reductions provided for in tax law provisions. Their application reduces the tax

2 See bibliography items mentioned above.

base or the amount of tax itself. Tax relief is not a reduction of the amount of output tax by the amount of input tax, resulting from one of structural principles of VAT, i.e. the principle of deductibility (Tax Ordinance Act, Art. 3/6 *in fne*). Tax relief is not other deductions forming part of the structure of this tax. The provision, which serves as a source of reconstruction of the norm which defines tax relief is included in Chapter I "General provisions" of the Tax Ordinance Act. The use of one of directives of systematic interpretation i.e. *argumentum a rubrica*, implies treating it as a common definition for the whole legal system. Thus, it is necessary not only for the reconstruction of legal norms from the provisions of the Tax Ordinance Act, but also other legal acts, including tax laws (cf. Mastalski, 2017: 51–52)[3].

In the course of legal interpretation, reconstruction of a tax relief from the provisions of the Tax Ordinance Act in the sense under Article 3 section 6 of the Tax Ordinance Act requires *prima facie* to fulfil cumulatively three conditions. These include, first of all, finding that tax law provisions being interpreted uses one of the terms such as: exemption, deduction, abatement or reduction. Second, the ascertaining that the application of the act results in a reduction of the tax base or the amount of tax. Thirdly, the finding that an exemption, deduction, abatement or reduction does not constitute a reduction in the amount of output tax by the amount of input tax or other deduction which is a structural part of this tax (Mastalski, 2017: 51–52). If these conditions are met cumulatively in a given tax, then the legal construct concerned can be considered a tax relief.

In view of the analysis of Article 3 section 6 of the Tax Ordinance Act, the definition of tax relief also lists specific forms of tax relief. First of them is tax exemption. Although tax exemptions are distinguished from tax reliefs in scholarly terms, tax exemption is not a distinct legal construct under the discussed provision of the Tax Ordinance Act (cf. Bogucka-Felczak, 2019; Hanusz, 2015: 96; Etel, 2005: 34; Gomułowicz, 2004: 137–138; Nykiel, 2002: 8; Kurowski, 1970: 114). It is just a form of tax relief (Hanusz, 2015: 96). Apart from exemption, the forms of tax relief mentioned

3 Other, incorrect view, cf.: Bogucka-Felczak, 2019; Nykiel, 2002: 8. They point out that the norm contained in Article 3 section 6 of the Tax Ordinance Act defining the tax relief is not universal in nature for the legal system. However, as has already been mentioned, this is not a correct view in the light of the rules of interpretation of the law.

in Article 3 section 6 of the Tax Ordinance Act are deductions, reductions and abatements. It can be generally referred to as discounts (Gomułowicz, 2004: 137; Kostecki, 1985: 201; Kurowski, 1970: 114). Importantly, the norm defining tax relief does not suggest that the application of a tax exemption or reduction, deduction or abatement is to constitute an embodiment of taxpayer's right or obligation imposed on him by tax law. However, when dealing with tax planning, the taxpayer's conduct should be emphasized. Such conduct constitutes tax planning where the taxpayer uses the means provided for by the legislature, which establish a right to reduce taxation. A legal norm construed from the tax law provisions governing a means allowing the taxpayer to reduce his tax burden should therefore contain a permission, not an order or prohibition of a specific conduct. Therefore, in order to determine whether tax exemptions and tax discounts are used for tax planning, their essence should be examined.

3 Tax exemptions and tax planning

The first form of tax relief, within the meaning of Article 3 section 6 of the Tax Ordinance Act, is tax exemption. The scholarly literature points out that the essence of tax exemption is that although certain factual states fall within the subjective and objective scope of the obligation to pay a particular tax, the legislator has decided to move them out of the scope of taxation (Hanusz, 2015: 51; Hanusz, 2006a: 26 et seq.; Hanusz, 2006b: 31 et. seq.; Gomułowicz, 2004: 137). Thus, it entails a limitation in the subjective or objective scope of the tax concerned. A tax exemption results in the lack of legal possibilities to concretize a tax obligation as a tax liability, so no tax liability is created in consequence[4]. Even though a certain factual state meets the criteria of a tax factual state and therefore remain of interest to the legislature, it is, for certain reasons, treated as an exception in relation to the general framework of the tax concerned (Hanusz, 2015: 51; Hanusz,

4 A tax obligation, within the meaning of Article 4 of the Tax Ordinance Act, is the unspecified obligation to make a forced payment resulting from tax acts in connection with the occurrence of an event specified in these acts. Whereas pursuant to Article 5 of the Tax Ordinance Act a tax liability is a taxpayer's liability resulting from a tax obligation to pay to the Skarb Państwa, województwo, powiat, gmina a tax in the amount, on the date and place specified in the tax law provisions.

2006a: 26 et seq.; Hanusz, 2006b: 31 et. seq.; Gomułowicz, 2004: 137). Covering a certain group of taxable persons with an exemption, due to their certain characteristics, allows for distinguishing subjective exemptions (cf. Hanusz, 2015: 52; Etel, 2005: 35; Nykiel, 2002: 16; Kostecki, 1985: 160–161; Kurowski, 1970: 114). However, certain features of the object of taxation, such as the manner of using it, or allocation of revenue, income or assets, justify the introduction of objective exemptions (cf. Hanusz, 2015: 52; Etel, 2005: 35; Nykiel, 2002: 16; Kostecki, 1985: 160–161; Kurowski, 1970: 114).

As mentioned above, the scholarly literature specifies tax exemptions as a means of tax planning. In a general and abstract legal norm construed from the provisions of a tax law, they are situated in its hypothesis (a set of prerequisites for a conduct covered by the norm to occur) specifying the conditions for the application of the exemption. Thus tax exemption fully restricts the scope of a norm construed from the provisions of tax law. Where a subjective exemption is applied, the range of addressees of the norm, defined in the hypothesis of a general and abstract legal norm rooted in the provisions of tax law, is limited. On the other hand, objective exemption narrows the area of factual states, the occurrence of which causes the fulfillment of the precept of specific conduct contained in the general and abstract norm. This precept is a duty to pay tax.

Tax exemption means a limitation, assumed by the legislator, of the subjective or objective scope the tax liability. Therefore, in the case of tax exemption, the taxpayer must not influence, through his conduct, the establishment or waiver of the exemption as a tax planning means. The subjective or objective scope of the tax is limited by operation of law. The use of exemptions provided for law may be either obligatory or optional. The first is, for example, the exemption under Article 43 paragraph 1 section 18 of the Act of 11 March 2004 on the Tax on Goods and Services. This provision governs an exemption from the tax in terms of medical care services. If the conditions for applying the exemption are fulfilled, i.e. provision of medical services by a medical operator, as part of medical activity, for health prevention, preservation, rescue, restoration and recovery, then these services are exempted from taxation ex officio, without a request from the taxpayer (cf. Michalik, 2018). Therefore, a medical operator cannot directly affect

the application of the exemption by its action or non-action. These services are, by operation of law, exempt from the tax on goods and services. Thus, considering the essence of tax exemptions, there is no reason to argue that tax planning is manifested in the application of tax exemptions.

It should be noted however that tax law provisions mostly regulate tax exemptions that are applied by operation of law. However, there are few exceptions that allow concluding that tax planning is manifested in the application of tax exemptions. They are tax exemptions which include a taxpayer's right to make a choice concerning taxation. It is a right of either not to use an exemption or to use it. An example of exemption with a right to renounce using it is the subjective exemption in the tax on goods and services. Pursuant to Article 113 of the Act on Tax on Goods and Services, the subject to exemption is sales by taxpayers whose value of sales in the previous tax year has not exceeded the amount of PLN 200 000 in total. However, the taxpayer, if he meets certain conditions, is entitled to waive this exemption.

On the other hand, an example of tax exemption that contains a right without the obligation to apply it is an exemption regulated by the provisions of Article 4a of the Act of 28 July 1983 on Inheritance and Donation Tax. The acquisition of property or property rights by the spouse, descendants, ascendants, stepchildren, siblings, stepfather and stepmother of the deceased is exempt from inheritance and donation tax, if these persons fulfill the conditions set out in the provisions of Article 4a of the Inheritance and Donation Tax Act. Otherwise, gratuitous acquisition of particular assets from these entities is subject to taxation. As we can see, not all exemptions, but only those tax exemptions that in their design contain a right can be a means of tax planning. Only then can the taxpayer influence the amount of tax burden.

4 Tax discounts and tax planning

Apart from exemption, the forms of tax relief include also deductions, reductions and abatements within the meaning of Article 3 section 6 of the Tax Ordinance Act, cumulatively referred to as discounts (cf. Gomułowicz,

2004: 137; Kostecki, 1985: 201; Kurowski, 1970: 114). Unlike tax exemption, the common feature of tax deductions, reductions or abatements is the result of their application. They always reduce the tax base or the amount of tax. Therefore, the tax deductions, reductions and abatements listed in Article 3 section 6 of the Tax Ordinance Act, bring the norm defining the tax relief most close to its theoretical concept. It is emphasized by scholars of law that tax discounts do not mean that the legislature has given up taxation of specific entities or factual states, but they are connected only with a reduction of the tax burden resulting from a specific tax liability (Gomułowicz, 2004: 137). So they can *prima facie* be used for tax planning. Although the final result of applying a tax discount is reduction in the amount of tax to be paid, three types of them should be distinguished: those which reduce the tax base, those which reduce the tax rate and those which reduce the amount of tax (Hanusz, 2015: 96; Etel, 2005: 35; Gomułowicz, 2004: 137).

In the light of the norm defining tax relief, a tax discount causing a reduction in the tax base or the amount of tax may result from two situations. They depend on the rule of conduct expressed in a disposition of legal norm construed from the provisions tax law which regulates the tax discount. On the one hand, it may express an order to reduce the tax base, tax rate or amount of tax. This discount will then not be used for tax planning. This is so because the taxpayer will be obliged to make such a reduction. On the other hand, disposition of such norm does not need to require or prohibit the reduction of the tax base, tax rates or tax amounts, but only allow doing so. In other words, it may indicate that a specific action is allowed if the conditions set out in the hypothesis of this norm are fulfilled. A discount which grants taxpayers the right to reduce the taxation may therefore allow tax planning. The ascertainment that it constitutes a tax planning means is therefore dependent on the content of the provisions of tax law which regulate a particular tax relief.

The analysis of the provisions of tax laws indicates that not all tax discounts are the result of a taxpayer's right to reduce the tax base or tax amount. Very often the provisions of tax laws use terms which suggest that the taxpayer

is obliged to make a deduction[5]. The reconstruction of a legal norm from the provisions governing a tax discount made according to the rules of linguistic interpretation may not, however, prejudge that the deduction is a taxpayer's duty. Even if wording of the act uses this phrase. Only the application of the rules of systematic, teleological, and functional interpretation allows for correct determination of the model of conduct in the disposition of legal norm being construed.

For example, the deduction of eligible costs by a taxpayer running a R & D business from the tax base of the natural persons income tax is a kind of tax planning. Pursuant to the literal wording of Article 26e paragraph 1 of the Act of 26 July 1991 on Natural Persons Income Tax, a taxpayer earning income from economic activity shall deduct from the tax base the tax deductible expenses incurred on R & D activities, referred to as "eligible costs". The taxpayer does so if he fulfills the conditions laid down in Article 26e of the Natural Persons Income Tax Act. However, unlike the result of the linguistic interpretation, the deduction of eligible costs from the tax base is not required but permitted by the legal norm. The *ratio legis* of Article 26e of the Natural Persons Income Tax Act indicates that it is supposed to implement a tax preference for entrepreneurs running R & D activities. This is to create the option of deducting from the tax base the tax deductible costs incurred by the taxpayer for research and development, namely eligible costs (cf. the explanatory note for the draft Act on the amendment of certain laws in connection with the promotion of innovation activities, 7th term of the Sejm, Sejm Papers No. 3286). It is only referring to the purpose of the legislation which makes it possible to conclude that Article 26e of the Natural Persons Income Tax Act creates a taxpayer's right, not obligation, to deduct eligible costs. It may therefore constitute a means for tax planning.

On the other hand, the deduction of health insurance contributions from the amount of natural persons income tax under Article 27b of the Natural Persons Income Tax Act is not tax planning. Although it qualifies as a tax relief within the meaning of Article 3 section 6 of the Tax

5 For example: "the taxpayer shall deduct (reduce)"; "the tax shall be subject to reduction"; "the rate shall be subject to deduction".

Ordinance Act, it does not create the taxpayer's right to make a deduction, but an obligation to do so. The phrase "income tax is first reduced by the health insurance contribution" reconstructed by rules of a linguistic interpretation means that the taxpayer is required to make that deduction (cf. Modzelewski, 2018; Bartosiewicz, 2015; Regional Administrative Court of Łódź: I SA/Łd 931/13). However, the health insurance contribution is not deductible in whole amount, but in 7,75 % of the basis for its calculation (Natural Persons Income Tax Act, Art. 27b/2). However, the remaining amount, i.e. 1,25 %, is financed from the taxpayer's income. On the other hand, the application of the rules of external systematic interpretation requires the reference to the provision of Article 95 paragraph 1 of the Act of 27 August 2004 on Public-funded Health Care Services. Pursuant to this provision, the health insurance contribution is deductible from personal income tax under the conditions set out in the Natural Persons Income Tax Act. The requirement to reduce the amount of tax by the health insurance contribution implements also the purpose of the provisions governing the structure of the health care system. Generally, the idea is that the health insurance contribution is to be financed from the personal income of the insured. The larger part of the contribution is then deducted from the amount of natural persons income tax, while the other part of the contribution is to be covered from the income of the insured (cf. the explanatory note for the draft Act on public-funded health care services, 4th term of the Sejm, Sejm Papers No 2976). Apparently, this relief clearly does not serve tax planning.

5 Conclusion

The aim of this paper in the form of an analysis of tax reliefs, within the meaning of the provision of the Tax Ordinance, in the process of tax planning, was achieved. It was ascertained that due to the use of means allowing the taxpayer to reduce his tax burden, which in their concept include the right to use them, the taxpayer may mitigate taxation as part of tax planning. However, this is not applicable when a disposition of legal norm derived from the provisions regulating this type of means determines the order or prohibition of a specific behavior. Therefore, the hypothesis

that not every form of tax relief within the meaning of Article 3 section 6 of the Tax Ordinance Act is a means which entitles the taxpayer to reduce, as part of tax planning, was confirmed.

Tax exemption, as one of the forms of tax relief within the meaning of Article 3 section 6 of the Tax Ordinance Act, is generally applicable by operation of law. Its construction does not allow the taxpayer to reduce his tax burden with his purposeful action. On the other hand, tax discounts, as the second form of tax relief, allow tax planning only if they entitle the taxpayer to reduce the tax base or the amount of tax. *De lege lata*, the tax law provisions contain tax reliefs that both may be used for tax planning and those excluding such use.

The legislative correctness of the provisions governing tax discounts raise some objections. From the point of view of certainty of legal transactions, they should unequivocally express either an order or permission to reduce the tax base, the tax rate or the amount of tax. Therefore, it is necessary to postulate *de lege ferenda* that the right to make a tax discount be expressed in the text of a legal act by the phrase: "is entitled to" or "may". Whereas, an order to reduce the tax base, tax rate or tax amount should be formulated using the phrases "shall be obliged" or "shall be reduced".

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Joint and Several Liability in Tax Law in the Draft of a New Polish Codification of General Tax Law

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Abstract

The study depicts legal solutions referring to chargeability and fulfillment of joint and several tax obligations. This issue has been regulated in the draft of a new Polish Tax Ordinance prepared by the Ministry of Finance and General Taxation Law Codification Committee appointed by the Polish Prime Minister. A main purpose of the study is to present essential assumptions the new regulation of the above mentioned institution has been founded upon. Complexity of the discussed subject matter justifies a broader analysis of not too extensive set of provisions related to joint and several liability in tax law. This study has been mainly prepared with the use of a formal dogmatic method.

Keywords: Taxes; Law; Tax Code; General Tax Law; Joint and Several Liability.

JEL Classification: H34.

1 Introduction

Due to its intrusive nature, tax law is a part of public law (Etel, 2010: 343). In many areas, however, tax law relies on legal institutions derived from private law (Goettel, Lemonnier, 2011). This applies, among other things, to joint and several obligations. The provisions of the Act of 23 April 1964 – the Civil Code[2], regulate this issue in the Polish legal order. As far as joint and several (passive) liability of debtors is concerned, each of them is obliged to a creditor to honor the obligation in whole as if he or she was one debtor. A creditor, on the other hand, may – at his or her discretion – demand

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2 Uniform text: Journal of Laws of 2018, item 1025, as amended.

payment of the whole or partial obligation jointly from all debtors, from some of them, or separately from each of them. With regard to joint and several (active) liability of creditors, some of them may be entitled in such a way that a debtor may honor the obligation in whole to one of the creditors while the repayment of any creditor shall extinguish debt owed to all of them. At his or her discretion, a debtor may honor the obligation to any joint and several creditor.

The Polish tax law mainly applies the institution of joint and several debtors (Dowgier, 2017: 687). This solution vests tax authorities with a considerable power while their position as creditors in joint and several liability for tax obligations is significantly strengthened. The analysis of special tax law provisions envisaging such powers leads to the following conclusion: the Polish legislator uses them as a kind of peculiar sanction on the one hand, while on the other hand, it is applied as a method of levying tax in cases where there is more than one obligor.

For instance, in the context of a quasi-sanction, debtors' joint and several liability is used in the area of alternative liability of a specific category of entities (the so-called third persons) for tax arrears of taxpayers they are related to as family members, through shared property or capital[3].

Furthermore, this type of liability is very common in taxes burdening the real estate ownership (a real estate tax, agricultural and forest tax) when there are numerous taxpayers (co-owners or co-holders). In this case, the legislator decided that joint property justifies the application of rules on joint and several liability.

Generally, it is possible to indicate a number of cases where the Polish legislator takes advantage of the analyzed institution, which apparently entails its considerable importance in tax law. Hence, just for this reason, it has been restructured in the draft of a new Tax Ordinance, which is subject to advanced works carried out within the Ministry of Finance[4]. A purpose of this text is to present basic solutions within the above scope.

3 See Art. 107–118 of the Act of 29 August 1997 – Tax Ordinance (uniform text: Journal of Laws of 2018, item 800 as amended).

4 The Draft of 21 December 2018. Available at: https://legislacja.rcl.gov.pl/projekt/12314054

2 Primary drawbacks of the currently valid model of joint and several liability in tax law

Under the valid legal status, the issue of joint and several liability in tax law is regulated in Art. 91–92 of Tax Ordinance of 1997. The very title of Chapter 13 thereof, i.e. "Joint and Several Liability", is already inadequate to the problem under regulation because joint and several liability in tax law arises as early as at the moment of tax obligation's chargeability, fulfillment and, eventually, liability for the incurred obligation. Secondly, Art. 91 of the above-mentioned Act introduces the rule according to which Civil Code provisions on tax obligations are applied to joint and several liability for tax obligations whereas Art. 92 § 4 refers correspondingly to the provisions on civil law liabilities. These references do not envisage the application of those regulations appropriately, i.e. by taking into account tax law specificity, but directly, which in practice raises interpretative doubts connected with simple transposition of civil law to tax law (Dowgier, 2017: 2).

These two above-mentioned principal deficiencies of the binding provisions have been eliminated in the draft of a new Tax Ordinance. The provisions referring to the discussed subject matter have been included in Art. 290–293. These regulations have been placed in Chapter 13, Section II titled "Fulfillment of Joint and Several Liabilities". Art. 293 of the draft, on the other hand, contains a reference to the exclusively appropriate application of Civil Code provisions on joint and several obligations as well as liabilities for excess tax refund within the scope that is not regulated in Chapter 13. Such a legislative solution has emphasized the fact that tax law, in principle, has its own structure of joint and several liability that is occasionally modified in comparison to civil law regulations. Hence, the application of Civil law provisions will be solely alternative. It will be particularly apparent on the basis of the application of tax reliefs, exemptions and exclusions regulated in Art. 292 of the draft, which will be further discussed in this study.

Moreover, it should be noticed that the institution of joint and several liability in Polish tax law embraces different categories of obliged entities other than taxpayers. Under Art. 292 § 7, solutions envisaged in the draft of a new

Tax Ordinance will also apply to taxpayer's heirs, legatees 'by vindication' or individuals liable for the cost of tax proceedings. Furthermore, within the limited scope, new provisions are applied to third parties liable for tax arrears. Under Art. 12 of the draft, "*A third party is a person who, under the principles resulting from the statute, is liable for tax arrears of a taxpayer, tax remitter, and tax collector, or for tax arrears taken over by a legal successor*". Above all, if these entities are granted tax preferences, the obligation itself shall not be reduced – it shall be paid by other joint and several obligors. Such a solution has been considered reasonable because the nature of third parties' liability for tax arrears is alternative with regard to the original debtor. Furthermore, there have been no grounds for restricting tax authorities to enforce the entire tax obligation from such obligors.

3 General rules

The following rule with no exception whatsoever has been adopted in the drafted provisions: tax obligation, tax liability, liability for tax obligation or tax arrears, the right to excess payment or tax refund are of joint and several nature if it is provided by the Tax Law (Art. 290 § 1). It explicitly results from the above that the issue of joint and several liability cannot be merely limited to liability itself because it is essentially a result of the tax obligation and the ensuing liability as shaped by the legislator in a joint and several manner (Etel, 2017: 383). What is more, considering the fact that historically the Polish science of tax law has distinguished two manners of tax obligations' chargeability, i.e. by virtue of a statutory law or by service of a decision, the rule adopted accordingly stipulates that with regard to the latter situation, a joint and several liability shall arise only if a decision is served to all obligors. There is no exception to this principle as well, which is a result of the abolishment of a situation envisaged in Art. 92 § 2 of Tax Ordinance where, with regard to tax obligations collected in a form of joint pecuniary obligation, the rules on joint and several liability for tax obligation could be applied already when a decision has been served to one of the taxpayers[5]. It has been decided accordingly that only such a solution

5 It refers to situations where a tax authority charges a taxpayer with two or more taxes contained in one decision (agricultural, forest and real estate tax).

sufficiently protects the interests of those taxpayers obliged to pay tax who do not even have a decision establishing the tax. Although an order for payment is a form of a decision encompassing two or three taxes, this very fact is not a sufficient justification for such special rules on liability for tax obligation as those that are currently binding (Etel, 2017: 385).

A certain dilemma occurred when the provisions were created. It was connected with regulations on spouses subject to joint tax for their total income on the basis of the Act of 26 July 1991 on Income Tax on Natural Persons[6] which were upheld in the act of general tax law. Binding provisions of Art. 92 § 3 and 3a of Tax Ordinance of 1997 referring to such entities introduce joint and several liability both for the tax obligation and refund of excess tax. The authors of a new Tax Ordinance followed a general rule according to which regulations referring exclusively to a given tax shall not be contained therein, which would be an argument in favor of transferring the above-mentioned rules to the Act on Income Tax. It has been eventually decided, however, that these regulations may be applied more broadly, i.e. not only on the basis of income tax. In particular, the following opinion has appeared in administrative courts' case law: under the norm of Art. 92 § 3a, excess tax that arose from income tax may be credited for tax obligations or tax arrears of one of the spouses in other taxes[7]. In the wake of the above, if the regulation on joint and several liability of spouses was included in the Act on Income Tax, it could ensue doubts as to the legitimacy of the opinion expressed by the administrative court.

4 Instrumental obligations

One of the crucial defects of the binding Tax Ordinance is that its regulations completely omit legal solutions concerning the fulfillment of an instrumental obligation to submit a declaration[8] in the case of a joint and several

6 Uniform text: Journal of Laws of 2018, item 1509, as amended.

7 The ruling of Supreme Administrative Court of 12 September 2017 (I FSK 2199/15), Central Base of Administrative Courts Rulings. Available at: http://orzeczenia.nsa.gov.pl/cbo/query

8 Pursuant to Art. 13 point 4 of the draft, the term declaration also embraces tax returns, lists, comparisons, reports, statements, notifications and information that must be submitted by taxpayers or other entities under the provisions of lax law.

tax obligation or right (Etel, 2015: 307). Hence, Art. 291 of the draft contains a proposal to regulate this issue by indicating that with regard to a tax obligation and the right to excess tax refund or the right to tax refund that are joint and several in nature and ensue the obligation to submit a declaration, such an obligation must, in principle, be fulfilled separately by every taxpayer. Therefore, each of them submits a declaration required by the law himself while it shall exert legal effects solely in relation to him whereas other taxpayers shall not be exempt from fulfilling this obligation. By analogy, the correction of such a declaration does not exert any effect in relation to other obligors, who are not exempt from submitting the correction.

At an earlier stage of works on the draft, the above mentioned solution was supplemented by the provision saying that if a declaration was corrected by one of the taxpayers, a tax authority notified other taxpayers about the submitted correction and sent them a copy thereof. In principle, a purpose of such a solution was to facilitate the fulfillment of obligations burdening taxpayers, particularly in a situation when a declaration was corrected for individual reasons that some of other taxpayers were not aware of. What is more, as far as obligations arising under the law are concerned, an appropriate correction of the declaration by all joint and several taxpayers entailed that a tax authority would not have to carry out proceedings to determine an appropriate amount of the obligation.

However, in the wake of concerns raised by local governments representing municipal tax authorities, the drafted solution has been eventually abandoned. These entities claimed that it entailed an excessive amount of work in relation to anticipated results, particularly in such cases when a tax obligation arose through the service of a constitutive decision. In such a situation, even submission of information on a real estate, agricultural or forest tax did not close the case because a tax authority had to carry out the proceedings and issue a decision anyway. Therefore, notification about the correction would be an additional and costly obligation implemented during such proceedings.

5 Tax preferences

New provisions have regulated quite precisely broadly understood tax preferences referring to joint and several liabilities, which have not been included

in the currently valid legal order. As far as the above issue is concerned, the draft promoter departed from a classic approach to joint and several liability for tax obligations developed by the Civil Code provisions. The new regulation has been based on two fundamental assumptions[9]:

- a joint and several nature of a liability for tax obligations cannot in effect deprive an entity that fulfills statutorily determined prerequisites of the right to preferences,
- the application of preferences in relation to the obligor shall proportionally reduce obligatory payment burdening other taxpayers.

The implementation of the above mentioned guidelines entails a departure from the currently binding model of applying tax preferences to joint and several liabilities, which was based on a direct application of the Civil Code regulations and failed to include a specific nature of tax law. This has generated axiological doubts because in accordance with civil law (Art. 373 of the Civil Code), if a creditor exempts one joint and several debtor from debt or renounces joint and several liability, it does not exert any effect in relation to other debtors. Meanwhile one undivided joint and several tax obligation may expire in a way indicated in Art. 59 of Tax Ordinance (*inter alia* by payment, remission or limitation). For this reason, it was controversial to adopt the assumption resulting from a simple application of the Civil Code implying that against the rules of tax law, a tax obligation may expire solely in relation to one joint and several debtor while exerting no effect on other debtors.

On the other hand, as far as objective and subjective tax exemptions are concerned, according to the relevant case law, when one individual who is jointly and severally liable for tax obligation takes advantage of an exemption, the value of the tax should be reduced in proportion to the amount

9 They partly correspond to the solutions adopted in Art. 23 of the CIAT Tax Code Model (Centro Interamericano de Administraciones Tributarias – in the 1997 version of the Code (http://www.ciat.org/index.php/en/products-and-services/ciatdata/tax-rates/145.html?task=view), which indicates that the effect of joint liability is, among other things, that the exemption or remission of the obligation releases all the debtors, except when the benefit has been limited to a specific person. In this case, the tax authority may demand compliance from the others, with a proportional reduction for the benefited person's part.

he is liable for. Thus, other obligors shall be jointly and severally liable solely for the tax calculated as above[10].

Following the above-mentioned guidelines, Art. 292 § 1, 2 and 4 of the drafted Act has introduced a general rule, according to which if one jointly and severally liable taxpayer is exempted from tax, relinquished from tax collection or not subject to tax, the obligation shall be reduced by the amount he is liable for and burden only other taxpayers. It means that an entity taking advantage of the preferences shall not be obliged to pay the tax while this obligation shall burden solely a taxpayer who is not subject to this preference. Nevertheless, the latter one shall pay the tax that is appropriately reduced by the amount payable by the taxpayer covered by the preference. If two or more taxpayers who do not take advantage of preferences are obliged to pay tax, the amount of tax they are liable to shall be undivided – it will burden them jointly and severally.

This is the only assumption that will exclude a possibility of enforcing the whole tax liability from joint and several obligors who do not take advantage of tax preferences.

Bearing in mind different structures of taxes, it is not possible to presume beforehand which criterion will be taken into account to determine a reduced amount of the obligation. For this reason, the following term has been used in the draft to refer to the above issue: "*a reduction within the scope a given taxpayer is subject to*". This proportion will depend on the circumstances of a case; for instance, with regard to a real estate tax, it will be proportional to the share in the ownership, and if such a parameter does not exist, the presumption of equal proportions should be applied (Etel, 2017: 388).

Analogical rules have been adopted with regard to the relief to repay tax obligations involving remission. Both currently binding and drafted provisions of Tax Ordinance envisage remission that is a kind of relief to repay tax obligation as one of the inefficient manners of tax obligations' expiry. As a rule, it is granted upon a motion of the interested party in the form

10 The rulings of Supreme Administrative Court of: 27 June 2013, II FSK 2096/11; 5 March 2014, II FSK 748/12; 15 January 2015, II FSK 3012/12, Central Base of Administrative Courts Rulings. Available at: http://orzeczenia.nsa.gov.pl/cbo/query

of an individual decision issued if the prerequisite of an important interest of a taxpayer or public interest occur[11]. Therefore, the prerequisites of applying this preference are mainly of a personal nature, which should imply the following: firstly, other debtors are not a party to the proceedings on a relief initiated by one of joint and several debtors (Dzwonkowski, Zgierski, 2006: 692), secondly, if the applicant is exempt from debt, other taxpayers should not be affected by this. Nevertheless, an exception should be introduced to the latter rule according to which, analogically to other tax preferences applied to joint and several liabilities, remission shall reduce the tax obligation to be paid by taxpayers who are not covered by it.

As far as other categories of reliefs to repay tax obligations are concerned, i.e. payment in installments and deferred payment, it has been conceded that their effects should be limited solely to the applicant. In consequence, pursuant to Art. 292 § 6 of the draft, the application of these reliefs does not take effect in relation to other joint and several taxpayers.

6 Limitations of tax assessment and collection with regard to joint and several liabilities

The institution of limitation has been quite considerably restructured in the draft of a new Tax Ordinance. Most of all, the limitation of assessment and limitation of collection have been distinguished. Simply speaking, it can be assumed that the limitation of assessment is a period during which a tax authority will be entitled to question the correctness of tax settlement carried out by a taxpayer (e.g. in the submitted declaration) and issue a possible assessing decision if such a declaration is missing. The limitation of collection, on the other hand, results in the tax obligation's expiry, therefore, it is a period during which the obligation may be enforced (Etel, 2017: 253–282).

The drafted provisions envisage situations when time limits are modified by interruption or suspension of the course of running in both categories of limitations. Moreover, as far as joint and several tax liabilities are

11 Remission may also exceptionally occur without a motion unless there are statutory prerequisites to apply it, among other things, a lack of economic justification to carry out enforcement or taxpayer's liquidation.

concerned, it may happen that the limitation period shall begin to run on a different date for individual taxpayers.

Taking the above into account, the following assumption has been adopted in the draft: the limitation itself as well as the prerequisites of interruption and suspension of the course of running of a tax collection time limit that are of a personal nature and refer to one of the joint and several obligors should not affect a course of time limit in relation to other obligors. For this reason, pursuant to Art. 292 § 1 of the draft, the limitation of tax assessment and collection in relation to one of the joint and several taxpayers shall not generally produce effects in relation to other debtors, yet with the reservation that their tax obligation shall be reduced within the scope referring to the taxpayer who has been subject to limitation.

What is more, Art. 292 § 6 has adopted a rule according to which in the following situations time limits of tax collection shall be suspended or interrupted without affecting the limitation of liabilities of other joint and several taxpayers:

- the issue of a decision granting a relief to repay tax or deferring the time limit to submit a declaration;
- the service of a notice to proceed with security in cases specified in Art. 32a § 3 and Art. 35 § 2 of the Act of 17 June 1966 on Administrative Proceedings[12];
- setting up a mortgage or pledge;
- the declaration of insolvency of an obliged entity or initiation of restructuring proceedings in the meaning of the Act of 15 May 2015 – Restructuring Law[13];
- the application of the first enforcement measure if a taxpayer has been served a notice on its application before the lapse of the time limit of tax collection.

In consequence of the above solution, joint and several tax liability for tax obligation will embrace a situation where the tax collection limitation period will run differently for individual taxpayers. Nevertheless, the relevance of such a solution results from the fact that the event of a personalized

12 Uniform text: Journal of Laws of 2018, item 1314 as amended.
13 Uniform text: Journal of Laws of 2017, item 1508 as amended.

nature (e.g. proceeding with enforcement in relation to one of the obligors) should not affect the situation of other taxpayers.

7 Conclusion

To conclude the above considerations, it should be stated that the draft of a new Tax Ordinance is not a response to basic questions about the application of the institution of joint and several liability of debtors and creditors in tax law. This issue requires more profound reflection which, in my opinion, should result in a considerable restriction of applying these rules in tax law. Joint and several liability for tax obligation should be developed in an exceptional form rather than be generally applied in each case involving a larger number of debtors.

New provisions do not solve the above presented issues because their scope requires a special tax law review, which exceeds the scope of the general codification contained in the draft of a new Tax Ordinance. Nevertheless, with regard to the application of already binding rules, the new act solves the most significant problems, most of all within the sphere of applying tax preferences and limitation. With regard to the first area, it has been indicated that tax law considerably modifies a civil law concept of joint and several liability for the tax obligation by permitting its reduction. Hence, even though tax preferences of individual nature are directly applied only in relation to a given taxpayer, they indirectly affect the situation of other taxpayers as well. We should hope that these solutions will be approved of both by the practice and doctrine. However, we agree with Mrkývka and Czudek (2017), the frequency of changes in legal financial norms throughout their existence is significant and base alarming instability of financial law sector.

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Polish Tax Culture. An Attempt of Identification

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Abstract

Taxes are a complex and broad issue, and due to their scope, they are of interest to the general public, as they affect almost every aspect of life. This article is an attempt to take a broad look on tax issues and identify the characteristics of Polish tax culture. This requires an analysis of the cultural determinism of establishing and applying the law and of the legal awareness of taxpayers. The analysis of Polish tax culture in the 21st century is not only an assessment of tax issues but also a reflection on the direction of their development and changes.

Keywords: Tax; Law; Tax Culture.

JEL Classification: K34.

1 Introduction

Nerré (2008: 153) mentioned that there are two different kinds of tax culture have been identified: tax culture shocks and tax culture lags. The analysis of Polish tax culture in the 21st century is not only an assessment of tax issues but also a reflection on the direction of their development and changes. Each branch of the law contains culture-forming content and derives from culture (Tokarczyk, 2005: 103). If we accept the cultural entanglement of tax law, then this extended perspective will require an analysis of cultural determinism of the establishment and application of law and of the legal awareness of taxpayers.

Culture is one of the basic concepts of contemporary humanities (Kłoskowska, 1983: 9). It is above all a merging concept (Hopfinger, 2008: 23). By making a justified simplification, we assume that culture focuses on values and patterns of behavior, norms and ideas learned and

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passed down from one generation to the next, expressed in the products of material and immaterial human activity (Szczepański, 1978: 78). Culture is a group of norms and beliefs in people's consciousness regarding recommended behaviors and proper evaluations (Gromski, 2003: 60).

Law is one of the types of cultural norms (Zirk-Sadowski, 1998: 35). The links between law and culture are of a bilateral nature, because on the one hand, we talk about the cultural background of the law, and thus the influence of cultural factors on the specific content of the law, its form and application. On the other hand, we observe the influence of law on the culture of a given society, so the law can be seen as a culture-creating factor.

Recognizing the law as an element of culture does not eliminate the aspirations to develop a specific concept of legal culture (Gromski, 2003: 61). The term legal culture refers to the legal order, but also to the values, social knowledge, attitudes, and behavior towards this legal system. It is rooted in a specific culture, reflecting the problems of a society living in a specific area at a specific time. For the needs of the conducted research, we will assume that, on the one hand, the notion of legal culture includes in its subjective scope the attitude of all members of a given society towards the law and the attitude towards the law of those who create and apply it (Tokarczyk, 2008: 125; Tokarczyk 2007: 60–61). On the other hand, legal culture is expressed in the shaping of the legal system, taking into account experiences and accepted patterns (Pruszyński, 2006: 672). Therefore, it reflects the intentions and actions of the government and public authorities applying the law and the level of civic knowledge in the people that are governed (Pruszyński, 2006: 676).

2 Tax culture and constitutional norms

The pattern of Polish tax culture decoded from constitutional norms that should be implemented by the legislator, tax authorities and courts, and taxpayers is based on the values of equality, justice, the rule of law, universality and solidarity and the (economic) freedom of citizens, which can be limited in justified cases, in an adequate and legally specified form (Constitution, preamble and Art. 1, 2, 5, 7, 64, 84, 217). Tax culture results also from

the culture of the Polish Nation rooted in the Christian heritage of the Nation and human values (Constitution, preamble).

On the other hand, constitutional norms concern specific tax issues, however their practical meaning is negligible (Modzelewski, 2010: 88). They regulate only a few basic issues. Their main disadvantage is the lack of standards formulating the *tax rules* on the basis of which *tax* law should be created and applied (Kosikowski, 2006: 67). The Constitution of the Republic of Poland introduces the universality of taxation and exclusivity of the Act in the scope of establishing the obligation to bear burdens and public duties (Constitution, Art. 84). It also refers directly to the requirements regarding tax statutes (Constitution, Art. 217) and draft of law codes (Constitution, Art. 123 sec. 1). It also establishes the right of local governments to determine the amount of local taxes and charges in the scope specified in the Act (Constitution, Art. 168). In addition, taxes should also be referred to by other constitutional regulations that concern the general values, rights and obligations of citizens, protection of their rights as well as the system of sources of law and examination of the constitutionality of legal provisions.

An important shortage of tax culture in Poland is the lack of general instruments to protect individual and social interest. The constitutional legislator did not decide to introduce a tool that would constitute a mechanism for weighing these interests in tax regulations. The principle of a democratic state of law is too general and undefined to be able to fulfill this function. The legislator is limited by no prudence norm in the area of tax burdens.

3 Standards for the creation of tax regulations

We measure the culture of the legislator on the basis of using the tools of legal regulation in accordance with its nature, in a way that serves the proper performance of its functions (Szubert, 1983: 586). At the same time, the culture of the tax legislator is demonstrated by their resistance to modifying tax law regulations under the influence of ad hoc impulses to achieve current, particular benefits. The legislator should conduct a well-thought-out policy,

so that changes in the content of the provisions are justified by significant needs and do not occur too often[2].

The legislative procedure sets the institutional and procedural framework for the introduction of tax regulations and influences the shape of tax culture. However, reality shows that this process is susceptible to influences of pressure groups. In particular, it is involved in the implementation of ad hoc political objectives[3]. Interference with the content of tax law regulations under the influence of political impulses results in ill-considered regulations.

Lobbyists protect the interests of a particular group without caring about the interests of others, or costs are arising as a result of actions taken, such as breach of coherence or clarity of the content of the legal act. They have a significant impact on the shape of tax law, we can talk about the gradual privatization of the creation of tax regulations (Modzelewski, 2015: 409–411).

The culture of creating tax law shapes the tax culture to a large extent. The rational legislator is burdened with obligations that apply both to the examination of the applicable law and to the observation of facts that are not subject to applicable law (Kosikowski, 2006: 100). A normative obligation to monitor the operation of applicable tax regulations has not been imposed on the Polish legislator. Without such information, tax regulations are created in a random, ad hoc, and incidental manner, without concern for coherence and completeness of the tax law system (Kosikowski, 2006: 100).

The Constitutional Tribunal, like the doctrine, uses the principle of "decent legislation", deriving it from the broader scope of the principle of a democratic state of law[4]. The obligation for the legislator to follow the principle

2 See more on this subject: A. Gomułowicz, Podatki a etyka, Warszawa 2013, p. 70 and ff.; W. Szubert, Uwagi o kulturze prawnej [in:] Naród. Kultura. Osobowość. Księga poświęcona Profesorowi Józefowi Chałasińskiemu, Wrocław-Warszawa-Kraków-Gdańsk-Łódź, Wydawnictwo Polskiej Akademii Nauk 1983, p. 586.

3 See more on this subject: A. Gomułowicz, Lobbistyczny aspekt tworzenia prawa podatkowego [in:] Prawo finansowe i nauka prawa finansowego na przełomie wieków, A. Kostecki (red.), Kraków 2000, p. 79 and ff.; J. Głuchowski, Raport o stanie prawa podatkowego, [in:] Prawo finansowe i nauka prawa finansowego na przełomie wieków, A. Kostecki (red.), Kraków 2000, p. 113 and ff.

4 See: art. 2 of the Constitution and the case law, e.g. the judgment of the Constitutional Tribunal of 11 January 2000, reference number K. 7/99, OTK ZU No. 1/2000, item 2; Judgment of the Constitutional Tribunal of 20 November 2002, reference number K 41/00, OTK-A from 2002, no. 6, item 83.

of correct legislation is functionally connected with the principles of legal certainty and security as well as protection of trust in the state and the law. It introduces the requirement of specificity of provisions that must be formulated in a correct, precise, and clear manner (Constitutional Tribunal: K 7/99). They cannot cause uncertainty of its addressees as to their rights and obligations (Constitutional Tribunal: K 24/00 and 33/00). An important standard of tax legislation is also the prohibition of retroactive operation of tax law and the obligation to establish and observe an appropriate vacatio legis.

The law should be effective, achieve the set goals and not cause a situation where it implements unintended effects. The law should be not only effective, but also efficient.

In addition, the value of the tax system is its relative stability. The desired changes require adjusting the existing regulations, introducing new ones or eliminating those that were considered ineffective, inappropriate, unnecessary or misguided. However, changes in law always destabilize the legal order to a certain extent, and therefore should result from deliberate, prudent decisions. Changes that are influenced by temporary needs, most often motivated by political and populist reasons, must be perceived negatively.

Changes in tax law are most often of a fragmentary nature, often bear the mark of rush, and, as a result, Polish tax law is considered inconsistent and insufficiently communicative (Marianski, Nykiel, 2008: 8). In principle, it has become the rule to amend key (in terms of profitability) tax acts a few times per year[5]. Freedom of the legislator in creating tax law, a lot of ease in making changes to tax laws resulted in tax regulations introduced under the influence of impulse. Amendments became a legislative technique. Because it is possible to make amendments at any time, no plan for amending tax acts is being created.

5 For example, it can be pointed out that the Personal Income Tax Act (i.e. Journal of Laws of 2018, item 1509, as amended) was amended in 2015 15 times, in 2016 – 27 times, in 2017 – 20 times and by the end of July 2018 – 16 times. The Corporate Income Tax Act (i.e. Journal of Laws of 2018, item 1036 as amended) was amended in 2015 – 11 times, in 2016 15 times, in 2017 – 13 times, and by the end of July 2018 10 times. The Act on VAT (Value Added Tax) (i.e., Journal of Laws of 2017, item 1221, as amended) in 2015 was amended 6 times, in 2016 – 11 times, in 2017 – 6 times, and until the end of July 2018 – 9 times.

The tool restricting the freedom of the tax legislator is, although to a limited extent, the principle of a democratic state of law expressed in art. 2 of the Constitution. This imposes a way of thinking about the function and role of the state, including the field of tax legislation. However, its general character is too rarely an inspiration for the legislator, but rather constitutes an instrument of a subsequent nature, to assess the constitutionality of the adopted tax regulations.

4 Standards for the application of tax law

The concept of self-calculation of tax liabilities adopted in most taxes determines the manner in which the tax authorities and courts apply the law. The role of tax authorities is to check taxpayers' compliance with imposed tax obligations. In fact, in most cases, the law will be applied by the tax authorities when they come to the conclusion that taxpayers violated the norms of tax law. In turn, courts will apply tax law if taxpayers recognize that the actions of tax authorities infringe the law and take advantage of their right to challenge administrative acts in court.

The practice of applying tax law is shaped by many factors, in particular the correctness of tax regulations, but also the construction of the tax system and construction of the administrative structure and the level of education of employees of tax authorities and the general political climate. Additionally, case law and doctrine also have their influence on it.

Measures of tax culture in the sphere of application of law are the level of limitation of the arbitrary action of tax authorities, establishing the limits of their activity, and predictability of the results of applying the law. In addition, the value of the case law is to build a (relatively) uniform tax line. Both tax authorities and courts are supported by the scientific foundations of the doctrine.

Tax authorities and courts are expected to be active in the fight against law violations. They stand guard over the law. The relationship between taxpayers and tax administration authorities and administrative courts is determined by the trust in the efficiency of these bodies and the correctness of their functioning (Szubert, 1983: 581). If they represent a low culture

of action, and they are negatively assessed in the society or a source of disappointment, then it is the basis for shaping negative attitudes of taxpayers.

It is characteristic of the legal culture to conduct tax proceedings in a **very formal** way, strictly according to detailed legal norms (Thuronyi, 2003: 214). A certain degree of formalism of tax proceedings is necessary to ensure correct decisions (Szubert, 1983: 584). Procedural formalism, that is, among others, supposed to ensure reliability, impartiality and fairness of the decisions made, can be simultaneously seen as a tool to protect the taxpayer's rights and a way to ensure procedural fairness (Kmiecik, 2009: 179–180). But the overgrowth of formalism may lead to excessive length of proceedings. In addition, procedural correctness may violate the essence of the content of the decision.

Tax proceedings, regulated in the Tax Ordinance Act, are formalized, legal provisions impose, in given circumstances, the performance of activities in a certain way or involve certain consequences along with them (Czepita, 2008: 109–110). In this legal state, as stated by V. Thuronyi, taxpayers and their counselors focus on finding procedural errors committed by tax authorities, considering this tactic as a way of repealing the decision terminating such proceedings (Thuronyi, 2003: 214).

The legislator does not directly introduce tax obligations to protect the taxpayer's interest, however they secure the taxpayer's interest by introducing a number of legal regulations, in particular in the general tax law (Kowalska, Kowalska, 2011: 98). Guarantees protecting the taxpayer's interest are at the same time a commitment for the tax authorities to act in compliance with the taxpayer's rights (Kowalska, Kowalska, 2011: 97). The tax authority, as an entity acting in the interest of the general public, cannot act in a pro-fiscal manner, strive to satisfy an important public interest (Dębowska-Romanowska, 1998: 21–23) by breaching the taxpayer's rights (Kowalska, Kowalska, 2011: 98).

Tax proceedings are based on general principles (Pietrasz, 2010: 731). They have a fundamental impact on the way tax authorities operate. Thus, they have a special impact on building a tax culture in its aspect of applying tax law.

Administrative courts exercise control over the activities of public administration in terms of compliance of undertaken activities with the law. Therefore, it can be concluded that they protect taxpayers from the arbitrariness of decisions of tax authorities (Constitutional Tribunal: K 21/96) and from imposing unlawful obligations or limiting their rights (Pietrasz, 2010: 827).

In court-administrative proceedings, the court examines all issues related to the correctness of the decision made by the tax authority. The court examines whether the tax authorities have made correct findings regarding the validity of the applied legal norm, whether the standard has been properly interpreted, whether there is any doubt as to the factual findings and the taking of evidence and whether the tax proceedings complied with all legal standards. The consequence of this state of affairs should be the elimination by the court of all the relevant violations of the law, not only those that the complainant saw.

A complaint to the court does not in principle suspend the implementation of the decision, however, the legislator provided for the occurrence of situations in which it would be justified to suspend the implementation of the decision. The application of the institution of suspension of the implementation of the decision prevents damage to the taxpayer, so it seems that due to legal caution the tax authorities should suspend the implementation of the decision whenever there is no reasonable assumption that the taxpayer will take actions to prevent the execution of the decision.

An important consequence of the lack of legal stability is the depreciation of the tax case law (Stelmachowski, 2000: 28–31). By introducing changes to the applicable provisions, the decisions issued in the previous legal state are outdated. Meanwhile, the case law is important in correcting the content of the law and adapting it to the needs of life, shaping the content of law, and thus also in stabilizing the practice of applying the law (Glumińska-Pawlic, 2007: 240; Mastalski, 1993: 3; Stelmachowski, 2000: 29).

The skills of the tax authority and judges to understand tax law (also the "legal spirit") and applying it are important, though not very visible, factors shaping the tax culture.

5 Tax culture of tax payers

Research carried out at the legal culture level allows focusing also on the addressees of legal norms and their relation to their obligations and their rights (Szubert, 1983: 577). The process of transmitting and adopting specific cultural patterns is subject to norms and socially recognized goals (Kloskowska, 1983: 51). Under their influence in the historical experience of societies, certain types of behavior are eliminated or strengthened (Kloskowska, 1983: 51). The law-making process reflects and at the same time shapes attitudes towards law in society (Szubert, 1983: 578). The operation of tax authorities and the judiciary shapes in the society the attitude towards tax law and its assessment (Szubert, 1983: 578). In addition, the very attitude to law enforcement bodies is an important aspect of legal culture (Szubert, 1983: 582).

The legal culture of taxpayers is co-created by the level of legal awareness, which reflects the level of knowledge about law, attitudes towards law and the state of compliance with it, as well as assessments and expectations formulated by taxpayers.

Attitude towards the law is an element of legal awareness, shaped mainly by the knowledge of the applicable law (cognitive factor) and its assessment (emotional and evaluating factor). The emotional factor gives direction to the attitude, determines whether it is positive or negative. Attitudes towards tax law adopted by taxpayers belong to the individual's awareness, they express taxpayers' relations with the social environment.

Tax law assessments involve subjective feelings, positive or negative, towards the tax law. They depend on how extensive the knowledge of the taxpayer is, and to what extent it is true. The evaluation of the law covers its effectiveness and efficiency, compliance with the values it is to serve and the implementation of these values. There are different assessments of the applicable law and the impulses to act stemming from them. Respect for norms in the same way as rational calculation is the incentive of taxpayers' behavior, but sometimes there is an emotional response to a situation at the source (Frieske, 2001: 62).

Social conviction about the low quality of tax law is widespread. It is in the opinion of taxpayers burdened with numerous defects and shortcomings (Mariański, Nykiel, 2008: 8).

Taxpayers represent different attitudes, their common feature is the recognition of law as an important regulator of social life and, on the one hand, the conviction about the need to adapt their behavior to its requirements, and on the other hand, awareness of forced enforcement of tax law standards and the application of criminal measures. But an important factor is also the intrusive nature of tax law and the subjectively felt tax burden. It influences the taxpayer's attitude towards the tax obligation. The taxpayer acts rationally, makes choices using the maximization of wealth criterion, strives to achieve the greatest benefits (Niesiobędzka, 2013: 21).

Minimizing tax burden is a natural reaction of taxpayers (Niesiobędzka, 2013: 13–14; Pietrasz, 2007: 43; Sowiński 2009: 37–39). The reasons for taxpayers to take actions, both legal and illegal, aimed at minimizing tax burdens are not uniform. They should be looked for in four areas: moral, political, economic, and technical (Pietrasz, 2007: 44–45).

Tax mentality has characteristic conditions in each country (Richardson, 2007: 3–6). It is a derivative of historical conditions and the resulting relationship with the state and authorities themselves. It must be remembered that public and political life was under the control of the invaders, then the occupant, and then imposed and unaccepted authority. That is why resistance to any interference in private life has systematically developed. It is necessary to rebuild the taxpayers' tax culture.

6 Conclusions

The tax culture is built by three elements: the creation and application of tax law and the level of legal awareness of taxpayers. These three spheres of tax culture are permeating. They are based on values. The operation of the tax legislator and the bodies applying tax law shapes the legal consciousness and behavior of taxpayers, at the same time the behavior of taxpayers and their legal consciousness constitute a real fact that these entities must consider to be able to carry out their tasks (Szubert, 1983: 588). All aspects of the tax law culture are characterized by certain national differences.

The current position of M. Borucka-Arctowa remains that Poles are a society with very poor traditions of continuity of legal systems, national unity with the legislator, compliance with legal norms, and therefore we do not have the necessary conditions to create an overall social attitude and pressure of the public opinion towards respect and compliance with legal provisions (Borucka-Arctowa, 1967: 22–23).

In Polish conditions, the lack of continuity of the applicable law largely determines the shape of the tax culture. We are at the stage of building tradition, authority, and prestige of tax law. The legislator but also courts and tax authorities should be aware of this and their actions should be always taken in this context.

The political class should be aware of the price of creating a bad tax law, not only the political one (Gomułowicz, 2013: 71). Excessive politics in the legislative process lead to violations of the rules of reliable tax legislation. If the political instrumentalization of tax law assumes a permanent character, it results in the erosion of taxpayers' mentality and tax morality as well as that of tax authorities and the judiciary. It ruins the authority of tax law, and the loss of trust leads to the demobilization of action, discouragement, uncertainty (Borucka-Arctowa, 1998: 18).

Imperfections, problems, or doubts in tax law should be eliminated with due diligence, because lack of effectiveness or unintended results can cause far-reaching social consequences (Borucka-Arctowa, 1967: 22).

There is a widespread belief in both the doctrine and in the society of the low-quality of tax law. We bear the social costs of not having a permanent, uniform, simple, and understandable tax system. Taxpayers are not always sure about their tax and legal status. The tax risk of running a business in Poland is high.

Finally, it is necessary to notice that shaping the legal status of the taxpayer affects taxpayers' attitudes, their inclination to bear tax burden or to rather escape the tax burdens, so it is in the state's fiscal interest to care for the legal situation of taxpayers, so that they approve possible duties to the widest extent (Kiszka, 2003: 3).

Thinking about tax law in terms of its cultural determinants can change its perception, both by the legislator, law enforcement bodies and taxpayers. Tax law is faced with numerous problems. Although the expectations formulated in relation to tax law and culture are different, reflection on the role and significance of cultural factors can be inspiring. Let us hope that applying the cultural perspective will become the source of the desired change in thinking about taxes.

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Reducing the Costs of Tax Procedures in the new Tax Ordinance Bill

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Abstract

The aim of this publication is presenting regulations included in the draft of the new Tax Ordinance, the introduction of which will contribute to reducing costs of tax procedures. The assumption that was adopted as part of this study is based on the statement that in Poland these costs are too high. It results from the analysis of data in which the costs of tax procedures in Poland and in other countries are compared. In this paper, the following research hypotheses were adopted. First of all, the reason for too high costs results from excessively formalized and extended procedures of tax and fee collection the tax and fee collection. Second, Reducing these costs will contribute to a growth in tax revenues supporting the state budget and budgets local government units. Thirdly, the introduction of legal solutions planned in the draft of a new Tax Code will not reduce the legal protection of taxpayers.

Keywords: Tax; Tax Law; Tax Procedure; Tax Proceedings; Tax Ordinance Act; Costs.

JEL Classification: K34.

1 Introduction

One of two fundamental objectives which is to be implemented in the new Tax Ordinance is increasing the efficiency and effectiveness of tax assessment and collection (Etel, Popławski, Tax Codes, 2016: 78, Etel, Popławski,

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The assumptions, 2016: 15). The bill of the new Tax Ordinance was prepared by the General Taxation Law Codification Committee appointed in 2014. The bill was presented to the Minister of Finance 9 October 2017Efficiency is understood here as not only increase in budget revenues from taxes (Liska, 2018: 420). The term includes "pure profit" accounting for a difference between tax incomes and costs of their collection. Over the recent years in Poland, an emphasis is put on sealing the tax system, which primarily means eliminating "the tax gap" resulting from different forms (legal and illegal) of taxpayers' avoiding paying taxes. The designed regulations of the Tax Ordinance notice the problem and provides for instruments for their fighting, the aim of which is to reduce evasion and avoidance of tax paying, and, in effect, to increase tax revenues supporting the state budget and local government units (Radvan, 2017: 532) – the clause against taxation avoidance, reporting tax schemes and regulations serving to preventing the use of the financial system for frauds, the so-called STIR (McGee, R. W., Gelman, W., Tarangelo, T. J. 2014: 218). The improvement of the efficiency of tax collection is seen by the authors of the Tax Ordinance bill not only in increasing revenues. A very important element, particularly in Poland, is costs of the implementation of tax procedures, the aim of which is tax assessment and collection (Carnahan, 2015: 170–171). The evidence of the fact that the costs are high are various rankings, where Poland is in the forefront (Wyrzykowski, Kasprzak, 2017: 84–94). In accordance with the OECD report of 2015 (Tax Administration 2015), Poland has the third most costly tax administration of the world. The high costs of tax collection in Poland result from very formalized and excessively extended tax procedures, which must be implemented by the tax administration. The bill of the new Tax Ordinance proposes solutions aiming at reducing these costs (Etel, 2017: 28–35). The major ones are the subject of this article.

2 Procedures for trivial tax amounts

Seeking to reduce costs of procedures it is important to decidedly spread the rule, already in force in local government taxes, according to which the procedure is not initiated, and if already initiated, discontinued, when the tax amount does not exceed costs of the delivery of the decision

(e.g. Local Taxes and Fees of 12 January 1991, Art. 6/3a). The amount is too low (after rounding 7 PLN). The tax of a few zlotys just covers the costs of delivery, assuming that in the case only one tax decision is issued. What about other costs connected with the collection of such a tax? The tax the amount of which is lower than the costs of its execution has no economic justification. The Tax Office does not want such a tax and – which is understandable – the taxpayer. It is collected only because the tax law demands it. It is the beneficiary of the income from the tax who should decide when it is profitable for them to collect the tax. Otherwise, the taxes which have to be subsidized make a financial burden for the state budget or local government units (Radvan, 2019, Radvan, 2016: 515). The already mentioned draft of the new Tax Ordinance extends the rule of not initiating or discontinuing procedures for trivial amounts. In the case where the tax amount does not exceed 50 PLN, the procedure is not initiated and the already initiated one is discontinued, notifying the taxpayer (Etel, 2018: 375)

The procedure refers to the proceedings initiating (discontinued) ex officio. It cannot be applied by, for example, a taxpayer, who calculated in the declaration an amount lower than PLN 50. The amount resulting from the declaration must be paid. If the taxpayer fails to pay the authority may, on the basis of the declaration, initiate an executive procedure.

3 A simplified procedure

A problem negatively affecting the effectiveness of tax authorities is the necessity of conducting tax procedures referring to small tax amounts in obvious cases, which do not require conducting any evidence proceedings. There is no sense conducting a formalized and expensive procedure in the situation where the tax amount is not high, the facts raise no doubts and the taxpayer wants to have the case resolved as soon as possible (Alink, Kommer, 2011: 55). In the ordinance currently in force routine cases concerning PLN 100 have to be conducted in accordance with the same rules as the cases regarding PLN 10 million, which by nature require long evidence proceedings. This shows the need for introducing simplified procedures (Kmiecik, 2014: 8). Such procedures are deformalized and in principle must

be short. They are concluded with the decision which is does not require justification. In effect, the taxpayer has the decision soon, and the tax authority has less work and lower costs of proceedings. The simplified procedure cannot be implemented without the taxpayers's consent (or request), and in problematic cases, where occur discrepancies regarding the circumstances affecting the tax amount. The proposal of simplified procedures is included in the draft of the new Tax Ordinance (Popławski, 2017: 335). In accordance with the bill, if there is no need for evidence proceedings (facts do not raise any doubts) or the tax amount does not exceed 5 000 PLN, the tax authority my, at the party's consent, immediately issue a decision, which they do not justify. Cases in this procedure will be settled quickly, within no more than 14 days. In accordance with the bill, the simplification of the procedure narrows down to no need for issuing and delivering decisions of its initiation; the taxpayer is not notified about the possibility of expressing their opinion on the evidence material collected, and the decision issued is not justified, unless the party demands it after the decision is delivered. The tax payer has the right, based on general rules, to appeal against the decision of the tax authority and challenge the decision in court. The introduction of the simplified procedure in the draft of the new Tax Ordinance will improve settling petty cases, reduce the workload of the authorities and the costs connected therewith.

4 A representative procedure

The reduction of the procedure costs will be affected, in compliance with the new Tax Ordinance, by a possibility of suspending several procedures conducted in similar cases until the end of the representative procedure. The tax authority, on the party's request or ex officio may suspend the procedure when another procedure is in progress, and the factual circumstances of the cases or the problem in them is similar. In this way, instead of simultaneous conducting a few procedures regarding the same tax against one taxpayer for particular years, it is possible to wait for the resolution of, for instance, the court of the representative case, which will enable a swift settlement of the suspended cases.

5 Costs of communicating with the taxpayer

One of necessary conditions of reducing the costs of tax procedures is introducing a cheap and effective way of communicating the tax authority with the taxpayer and their representative. The delivery of a tax decision to the taxpayer should not be a costly and long procedure for the tax authority, sometimes preventing collection of huge tax amounts due to limitation. The bill proposes extending the possibility of delivery through electronic means of communication. Documents in this form will be allowed to be delivered not only to professional agents and public entities, but also entrepreneurs (except micro-entrepreneurs, unless they provide an electronic address), as well as users of electronic information and communication systems (e-PUAP and the tax portal). Additionally it proposes that the data pointed at in accountancy reports and stored in the Central Register of Taxpayers of the National Records of Taxpayers (CRP), constituted the basis for establishing the address of residence and the address of the business in order to deliver documents. The possibility of effective delivering to the address indicated in this register will increase the effectiveness of deliveries and reduce costs thereof. Taxpayers who fail to have an address indicated in CRP, documents will be delivered on the general principles.

6 A tax declaration

The taxpayer's own declaring a tax and its payment onto the account of the tax authority is undoubtedly the cheapest way of meeting tax obligations. Hence, in order to reduce the costs of tax procedures, it is necessary to increase the role of a tax declaration in the process of tax paying by the taxpayer. It would be the best, which is now impossible for different reasons, to eliminate from the system taxes arising after the delivery of the assessment decision. However, it is possible, and which is provided for the newly designed provisions of the new Tax Ordinance, to introduce solutions encouraging the taxpayer to submit the declaration and thereby to their own calculating the tax.

One of them is a possibility to correct the declaration in the last stage of the procedure, just before issuing a tax decision, within the period provided for

commenting on the collected evidence material. The taxpayer already knows what charges the tax authority has brought against their way of calculating the tax, and may, therefore, correct themselves their tax declaration before the authority issues a decision. In this way the tax procedure is terminated (the authority discontinues the procedure in the case of the approval of the tax amount resulting from the declaration); there will be no appeal procedure, which undoubtedly reduces the costs of a tax proceedings.

7 Non-ruling ways of settling tax cases

One of fundamental factors determining the number of tax procedures and their high costs is bad relations between tax authorities and taxpayers. This results from the fact that the vast majority of cases is conducted by a tax authority according to the following pattern: inspection, initiating the procedure, decision, execution, complaint to the administrative court. In this mode of settling a tax case, the taxpayer does not talk to the authority (an official), but there occurs an exchange of correspondence, which sometimes takes a few years. The currently binding regulations do not provide for any space for deformalized ways of solving tax problems, which are reduced to a conversation of the taxpayer with the official and agreeing on controversial issues. The current Tax Ordinance says nothing in this matter, which discourages both parties from taking attempts at such settling the cases. Tax officials are just afraid of settling a case in agreement with the taxpayer due to easily formulated charges of corruption. The bill provides for regulations which legalize the so-called non-ruling forms of settling tax cases (mediation, tax agreement, agreement of cooperation) and secure their implementation. They also oblige the official to provide the taxpayer with information in any form, including a conversation. The bill "legalizes" a talk of the official with the taxpayer, the establishments and information thereof are legally protected. The official has a right to come to an agreement with the taxpayer (e.g. regarding the number of installments into which the tax arrears are divided) without a fear of being charged with corruption, and the taxpayer who acquires information during the conversation with the official, will know that if they turn out untrue, they will bear no negative consequences of compliance therewith. Many cases (including tax cases) may be fastest

and most cheaply settled through talking and not exchanging letters, because this may last, as the practice shows, for years!

8 Combating the protracting nature of procedures

According to the current regulations, in each case of failure to settle the case on time, the tax authority is obligated to inform the taxpayer of the fact and to indicate a new date. The problem is that the indicated date does not have to be final and the authority may appoint another new data. This, among other things, results in the protracting character of procedures consisting in the tax authority's groundless lengthening the procedure, formally not infringing the law. They taxpayer is entitled to urge the authority but only in the case of failure to settle a case on time (the authority's inaction). In the new Tax Ordinance, also the delays in the procedure are a ground for submitting an urging reminder to a higher authority. Stating the occurrence of delays or inaction obligates the authority to appoint the final date of settling the case.

9 Resignation from the appeal against the decision in favor of a complaint to the court

The new ordination grants the taxpayer a right to resignation from an appeal against the decision of the tax authority. In accordance with the new regulations the party may resign from an appeal in favor of a complaint to the administrative court, unless they bring against the decision charges of infringing the rules of the procedure and question the facts which the authority recognized as proved, the evidence in which the court has believed, and the reasons why the authority refused credibility of other evidence, included in the justification of the decision (a charge of infringing substantive law). What can the taxpayer gain resigning from the appeal? Foremost, shortening the time of conducting the procedure by two instances (especially when in both instances the decision is made by the head of the custom-fiscal office). If the taxpayer does not believe that an appeal would result in anything, they may resign therefrom and directly forward the case to the administrative court.

10 Reducing the number of individual interpretations of the provisions of the tax law

The procedure operating in Poland of issuing by the Director of the National Revenue Administration individual tax interpretations at the request of the concerned results in situations, where until recently over 30 thousand interpretations a year have been issued. A possibility of complaining against these acts in administrative courts results in the courts overwhelmed with complaints, the consideration of which by the Supreme Administrative Court may take even two years. The effect of this state is not only generating considerable costs connected with issuing interpretations but also restricting judicial possibilities of administrative courts in other cases. The planned new Tax Ordinance proposes changes in this matter towards increasing the number and strengthening the role of general interpretations. The minister competent in public finance is obligated, in accordance with the bill, to issue with no unnecessary delay, a general interpretation in the case of a considerable number of requests for individual interpretations, referring the same facts or future events, submitted in the same legal state. Issuing such an interpretation limits considerably the number of individual interpretations, which is the aim of these changes.

In particularly complicated cases being subjects of a request for an individual interpretation, the bill proposes a higher fee: PLN 2 thousand. In the Ordinance currently in force the fee amounts in every case PLN 40, which is not commensurate with the costs of issuing an individual interpretation. Raising the fee in the most complex cases will not only contribute to compensate, to a certain degree, the costs but also reduce the number of requests.

Issuing general interpretations by the minister must be coordinated with judicial decision-making referring to similar legal problems. Therefore, the new provisions authorize the minister competent in public finance to direct the legal questions to the Supreme Administrative Court. The minister will be allowed to do so when, in the course of issuing a general interpretation, occur serious doubts in the context of divergent decisions of administrative courts.

11 Discontinuation of a tax

One of the forms of reliefs in the payment of tax obligations is discontinuing the tax arrears. In compliance with the currently valid regulations, a tax authority may discontinue the tax arrears, including the interest for the delay. Thus, the tax authority may discontinue merely the tax arrears (including the interest). Until the date of the tax payment and, therefore, tax arrears arise, the taxpayer cannot apply for the discontinuation. In practice it is an inconvenient situation not only for taxpayers but also tax authorities (Popławski, 2018: 465). The taxpayer has to wait with the request for the discontinuation until the deadline of the tax payment, which is related with late payment interests and fiscal criminal liability for the failure to pay the tax. The tax authority cannot discontinue the tax before its payment deadline, even though they know that the taxpayer meets the statutory criteria for discontinuation. This regulation is especially inconvenient in local government taxes arising by virtue of an establishing decision. For a wójt, mayor (president) must issue a tax decision, then deliver it, wait for the payment deadline and no sooner than that they may discontinue it, even though they know from the beginning that the taxpayer is not able to pay the tax. In local communities the tax authority employees know taxpayers very well and know that a few of them, for different reasons, are not able to pay the tax. Thus, why issue and deliver an assessment decision, wait for arrears to arise and issue another decision of discontinuing the tax in the situation where from the beginning it is known that the tax will not come to the budget of the municipality? There is no sense bearing the costs of preparing and delivering two decisions, since there is no chance obtain any tax payment. The bill of the new Ordinance proposes that the tax authority could discontinue not only the tax arrears but also the tax. Actually, the proposition consists in introducing, beside the discontinuation of the tax arrears, abandoning the tax collection. In this way, before the arrears arise the tax authority will be able to cancel the tax obligation through its discontinuation.

12 Recording of evidence proceedings with audio/video technologies

The planned Ordinance proposes a broader possibility of applying modern technologies of recording pictures and sounds, especially conducting evidence proceedings. Interrogations of the parties, witnesses, experts, the hearing, inspection, and other procedural activities conducted in the traditional way should be recorded (audio/video). This will allow for increasing the credibility of the evidence and will render the course of the activities more faithfully, which will allow for an objective assessment of its correct conducting by the appeal body or the court. This will minimize disputes in this matter, accelerate the evidence procedure and increase the effectiveness of the authority's operation. The carriers of the carried out activities, attached to the case files, will be an alternative for written protocols of interrogations and inspections. In the actual justification of the decision it will be sufficient to point at an appropriate fragment of the recording instead of extensive quoting the content of the evidence.

13 Conclusion

The assumption that was adopted as part of this paper was based on the claim that in Poland the costs of tax procedures are too high. It results from the analysis of data in which the costs of tax procedures occurring in Poland and in other countries were compared. It was presented that Poland has the third most costly tax administration of the world. Research hypotheses have also been confirmed. First, the reason for too high costs results from excessively formalized and extended procedures of tax and fee collection. Secondly, reducing these costs will contribute to a growth in tax revenues supporting the state budget and budgets local government units. Thirdly, the introduction of legal solutions planned in the draft new Tax Code will not reduce the legal protection of taxpayers.

This paper presented the major instruments proposed in the bill of the new Tax Ordinance for reducing the costs of tax collection. Among them, the following institutions will play a special role. First, tax procedures for trivial tax amounts will be employed in cases where the tax amount does not

exceed PLN 50. According to it the procedure is not initiated and the already initiated one is discontinued, notifying the taxpayer. Secondly, an important element will also be the introduction of a simplified procedure. The essence of this solution boils down to the fact that there will be no need for issuing and delivering decisions of its initiation. Moreover, the taxpayer is not notified about the possibility of expressing their opinion on the evidence material collected, and the decision issued is not justified, unless the party demands it after the decision is delivered. The third newly introduced institution will be non-ruling ways of settling tax cases. The bill provides for regulations which legalize the so-called non-ruling forms of settling tax cases (mediation, tax agreement, agreement of cooperation) and secure their implementation. It should be outlined that it is planned to increase the role of a tax declaration in the process of tax paying by the taxpayer. Designed provisions of the new Tax Ordinance, to introduce solutions enabling possibility to correct the declaration in the last stage of the procedure, just before issuing a tax decision, within the period provided for commenting on the collected evidence material.

The possibility to use of new Tax Ordinance by tax authorities will certainly contribute to more efficient and effective tax execution. We cannot concentrate on sealing the system only; it is important to simultaneously seek to reduce the costs of tax procedures. Only this comprehensive approach to the problem under scrutiny may bring the assumed results in form of increase in real budget incomes. The solutions proposed in the bill will contribute to considerable reduction of the costs. What is important to do is just implement them. This will be possible when employees of tax authorities are properly trained and receive support at the first stage of the application of the new regulations. This observation concerns especially innovatory institutions such as mediations, agreements and consultative procedures. Their real functioning depends on whether tax employees are not afraid of using them in practice. Even the best solutions fail to bring effects if they are not applied.

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PL: Local Taxes and Fees Act of 12 January 1991, as amended.

Legal Background for Taxation and VAT Drawback Fraud

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Abstract

VAT drawback fraud is by character against its nature. VAT is supposed to be a source of budget revenue for the state and local authorities. In Poland and the European Union, this is set in the constitution. Fraud surrounding VAT, the main source of tax revenue is contrary to the essence of the tax. There are different types of such fraud, which makes it difficult to detect and eliminate it. In the article we present the VAT regulations of the European Union and Poland, as well as the extent of losses caused by VAT fraud (VAT drawback) in Poland.

Keywords: Constitutional Tax Background; VAT Drawback Frauds.

JEL Classification: K34.

1 Introduction

By definition, tax means claiming a part of the financial resources from natural and legal persons for the benefit of the state and local budgets. Within the tax system, there is, inter alia, value added tax. Its structure enables the committing of drawback frauds. This fraudulent activity is observed, in various degrees, globally, causing billions in budgetary income being lost. The aim of this study is to present the analysis of the tax liability basis and the drawback fraud.

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2 Tax liability legal sources

Drawback fraud negates the essence of a tax itself which, in its core meaning. In its nature, a tax is contributed to the benefit of the entitled subject by the liable subject. The state is usually the entitled subject, also often referred to as the active subject. Moreover, local public law associations, such as states in federal countries, municipalities or rural communes, can also act as active subjects. International organizations can in some exceptions become active subjects if the member states enable them to impose taxes. (Głuchowski, 2002: 12).

There is a lack of a common binding definition of a tax. One of the most concise is that a tax is an individual donation for a collective cause (Grapperhause, 2010: 15). It is also commonly believed that there is a coincidence in this matter. This belief is absolutely justified. One of the most recent proofs in this case is the expertise included in the report presented during the European Association of Tax Law Professors congress, which took place in Naples (Caserta) (Barrassi, del Federico, 2005: 59–78).

It was also concluded that it is impossible to formulate such a definition of tax that will be constantly valid. It stems from the fact that taxes change simultaneously with the change in societies, their goals and initiatives. It was also pointed out that when the taxation process is being executed, it is wrong to focus exclusively on its income function. The aspect of keeping balance between the state interests connected with the budgetary income and protecting the individual's right to own a property, equal treatment and freedom is equally important (Suchy, 2005: 55–57).

The subject literature also includes reports connected to the concept of tax in EU law, the OECD model convention and the World Trade Organization (WTO) agreements.

Generally speaking, there are no definitions of tax in the EU law (Herrera, 2005: 207–226). Furthermore, member states are not obliged to use this term as it is formulated in directives (Selicato, 2005: 227–260). It is worth mentioning that the term tax is only used twice in the Sixth VAT Directive. Firstly, in the Article 33(1), this concerns, inter alia, taxes and duties. Secondly, it is mentioned in the Article 4(5), which refers to VAT, customs and charges.

The term 'tax' is used in the OECD Model Convention much more rarely than might be expected. When it appears, its meaning does not correspond to the definition. A study conducted on the convention's content indicates that the term 'tax' is used in tax treaties in Articles: 2, 24, 26, and 27. Surprisingly, the 'tax' definition does not appear in Article 2 of the Model Convention (Raad, 2005: 279–299).

As opposed to the OECD Model Convention, the term 'tax' appears in the World Trade Organization agreements more frequently than expected. In the three most significant WTO documents, i.e. the General Agreement on Tariffs and Trade (GATT), the General Agreement on Trade and Services (GATS) and the Agreement on Subsidies and Countervailing Measures (ASCM), the term 'tax' has been referred to 106 times in total. This can be explained by the fact that the WTO fights against discriminatory practices in trade, which may also include taxes. To clarify, the trade barriers may be established by means of taxes (Farrell, 2005: 301–304).

It is reasonable to presume that the obligation to pay taxes and the right of the state or other public law association to collect them ought to be legally authorised. At the same time, it has been stated that both the obligation and the right ought to receive the highest status, appear in Basic Law (Bourgeois, 2005a: 79–183) and gain identity (Bourgeois, 2005b: 185–196). In this regard, the coincidence of theory and practice is observed on a European and global scale.

In Poland, the obligation to incur fiscal and public charges is regulated by the Constitution (Dz. U. 1997, nr. 78, poz. 483) and was introduced on the basis of the Article 84. However, Article 2017 specifies that enforcing taxes, other public charges, defining taxable subjects objects, public rates together relief and remission regulations and types of tax exempt subjects are fulfilled by law. Thus, the rules that determine taxation stem from the political system (Gomułowicz, Małecki, 2013: 76).

In general, it needs to be concluded that the constitutional power enabling the imposing of taxes was first developed in Western Europe. Their range in those countries, and on a global scale as well, was determined by various factors. On the whole, the generally accepted principle is that the legislative

body is empowered to impose taxes and pass budgets and this procedure should have the form of an act.

Taxation regulations themselves are present in constitutions of particular countries to varying extents. Occasionally, they are limited to individual articles. On the other hand, they may also reach the size of the whole chapters (Głuchowski, 2002: 20–25).

From our point of view, it needs to be implied that the core meaning of a tax is a legitimate claim for part of resources on natural and legal persons to the benefit of the state and the mechanism is occasionally referred to as 'appropriation' (Brzeziński, 2000: 24–25). This is correlated with the fiscal function of a tax, whose essence is to claim public income.

Particular attention needs to be drawn to the fact that the amount of taxes claimed to the benefit of the budget needs to remain within the limits stemming from the Laffer curve. According to this concept, if taxes were not implemented, the state would not exist. However, if taxes consumed the whole income of a taxpayer, no-one would continue their profit-making activity (Eichenwald, 2017: 16–18). Therefore, the source of taxes should not be manipulated to the extent which could lead to critical extremes or total liquidation. In practice, fulfilling legitimate tax obligations is burdened by the activities connected with all taxes, but especially with one of them. The first is tax avoidance and evasion, the second being VAT drawback fraud.

To interpret the notion of tax drawback, the term of drawback fraud needs to be precisely defined. To fraud means "*to deceitfully and cunningly obtain something from somebody, to achieve*" (Dubisz, 2003: 625). The way in which the fraud was conducted needs to be defined as deceitful and including misleading instructions resembling the truth to such an extent (by means of witness statements, false documents or other evidence including the use of a third party as a substitute) that they convince the person issuing the document that they confirm the truth.

On the other hand, another dictionary suggests that to fraud means to deceitfully and cunningly obtain something, to request something from somebody. In Polish, one can "fraud' promises, privileges, gifts – and most importantly from our perspective – money (Szymczak, 1981: 817).

A fraud undertakes fraudulent actions in order to obtain a document confirming false but beneficial circumstances which have legal importance. At the same time, fraudulent behaviour may mislead the person issuing the document directly by providing false information or documents, or indirectly by, for instance confirming false information (Marek, 2010).

3 Tax drawback fraud

Tax drawback fraud results from imperfections in the settlement structure, especially concerning indirect taxes, which leads to a fraudulent criminal's benefit. In such a way, the criminals' aim is not only to evade paying a certain levy, but to obtain additional illegal benefit in the form of a tax drawback fraud. Moreover, although the criminals are mainly motivated to obtain from indirect tax drawbacks, they may also expect other accompanying benefits that they are not entitled to, such as understating their income tax (UN Global, 2016: 51).

Tax drawback itself is specified by tax law regulations. In practice it is connected with serious situations. Most of all, it can result from the tax deduction complying with the predetermined rate imposed on the income, while the earner is exempted from the tax or is entitled to a lower tax rate (Lyons, 1997: 400). Tax drawback is also applicable to excises and duties. However, in the majority of cases it applies to VAT. The right to receive a value added tax drawback is granted when the input tax exceeds the output tax. Furthermore, foreign entrepreneurs who are not residents of Poland are also entitled to receive it if they are obliged to pay VAT charged on expenses connected to their business activity, but only if they are not VAT payers in Poland and cannot make use of VAT settlement (Doorn-Olejnicka, 2014: 370).

An audit conducted by the Supreme Audit Office proves that the most significant irregularities were identified in terms of value added tax, introducing VAT invoices into economic circulation which did not reflect the real economic events, and deducting the tax charged on these invoices (Przeciwdziałanie…, 2016: 7).

A report by UN Global Compact also confirmed the position in this case which concludes that VAT drawback frauds, usually conducted on creating the chain of intra-community transactions, appear to be the most significant and still not completely solved problem (UN Global Compact, 2016: 79).

In practice, value added tax drawback fraud can be divided into two groups. The first concerns output tax fraud, and the second relates to the more frequent input tax and tax drawback fraud.

In the first group such forms of fraud appear as for example a goods delivery which de facto does not cross any borders but is declared as an intra-community delivery or export which has taken place but where the goods are worthless. Thus, the exports and their value are forged (fictitious action), the services provided on the domestic territory are eligible for the basic tax rate, but they are fictitiously declared as entitled to a 0 % rate or the reduced rate (lowered output tax). Furthermore, the services are provided on the domestic territory, but they are fictitiously declared as provided abroad (fictitious place of fulfillment) or the delivered goods are not enlisted in Annex no. 11 to the Act on Goods and Services Tax as those entitled to the "domestic" reverse charge (a fictitious lack of legal personality) (Raport…, 2014).

The aim of acquiring an undue benefit, the amount of which does not exceed the due output tax, but also avoiding paying tax liabilities, which leads to a negative impact on the budgetary income, continue to be the common feature of these activities.

The second group of value added tax drawback fraud is strictly connected with the structure of the tax itself, the input tax and the right to reduce the output tax amount by the input tax amount or the input tax drawback (the difference in the value of tax). This structure encourages some taxpayers to this abusive practice on an unprecedented scale.

In this group, such drawback or deduction fraud can be observed as: issuing "invoices" on activities which objectively took place by the existing subject which did not provide the service, but the taxpayer is another person; issuing "invoices" on services that did not take place; issuing invoices from a fictitious domestic or foreign subject, a so called 'missing trader', which was established purely with the view to issue these documents. Moreover,

another common practice is to issue invoices for a fictitious action, which objectively exists but simultaneously covers a different event, which in reality was a different transaction.

For many years, the audits conducted by the Supreme Audit Office and initiated by the Ministry of Finance, aimed at improving the efficiency of combating value added tax drawback fraud, limiting VAT drawback fraud and avoiding paying tax liabilities, are not fully satisfactory.

The solutions implemented to the taxation system in the last few years, including the reverse charge mechanism, joint and several liability and organizational solutions, have reduced the volume of irregularities concerning VAT drawback frauds. However, the implemented solutions prove to be insufficient in enhancing the efficiency to combat fraud committed by means of invoices not reflecting real transactions and also in reducing factors threatening the collection of state's budgetary income. The introduced changes, tightening up the VAT settlement system, concerned the identified irregularities exclusively. However, they have not reduced fraud and tax scams in a systemic way.

In the opinion of the Supreme Audit Office, instruments to combat tax fraud committed by means of invoices issued on fictitious activities need to be effectively introduced. According to the Supreme Audit Office, new solutions are essential to support in reducing the scale of this negative phenomenon, to support effective responses to threats as well as to punish fraud (Przeciwdziałanie, 2016: 13–14).

Organized crime that takes advantage of the value added tax structural regulations is a phenomenon of 1 January 1993, when the customs barriers between several UE Member States were abolished. As a result, the tax levy system (on imports) "on the state borders", which, as a rule, served as the basis for VAT settlement as far as the intra-community goods turnover is concerned, was abolished (Pabiański, Sliż, 2007: 18–27). To replace the terminated regulations, a solution based on taxation in the country of destination has been introduced and is in operation to this day. As a consequence, favourable conditions have emerged to develop VAT fraud schemes that are harmful to the states' budgets. Since goods were allowed to be relocated within the EU states. The taxation in the country of destination scheme

was launched in 1993 and there was no surveillance mechanism for member states (Ozóg, 2017: 20).

VAT drawback fraud is the cause of huge losses in the budget revenues of all EU member states. In Poland, in the years 2000–2017, these losses amounted to approximately EUR 10–12 billion annually. It should be unequivocally stated that VAT fraud is the biggest tax problem on a global scale.

4 Conclusion

Starting from the constitutional regulations, legal norms unambiguously oblige particular subjects to pay taxes. As a rule, the tax itself ought to be acquired to the benefit of the state. However, in practice, the tax appears to be used. This goal is frequently achieved by the means of value added tax drawback fraud. The proceeds from VAT settlements have multiplied revenues to a more significant extent than from any other form of tax. Simultaneously, the volume of losses equals to billions. A fraud undertakes fraudulent actions in order to obtain the document confirming the false but beneficial circumstances. The aim is not only to evade paying a certain levy, but to obtain additional illegal benefit in the form of a tax drawback.

Drawback frauds prove to not only be a problem concerning the European Union but are also present on a global scale. The means to eliminate them undertaken so far, have limited this phenomenon but have not absolutely eliminated it. Drawback fraud in Poland is not on a par with the experiences of the EU founding states. However, their experiences, accompanied with the experiences of other countries, are unquestionably valuable and ought to be broadly implemented in Polish and UE countries tax systems.

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Issues in Codification of Tax Law as Exemplified by EU-Members and Post-Soviet Non-EU Countries

Yulia Gorosh[1]

Abstract

The article highlights the approaches to the codification of substantive and procedural tax law that have developed in the EU member countries (Czech Republic, Poland) and post-Soviet countries that are not members of the EU (Russia, the Republic of Belarus). The analysis is carried out with the aim of revealing the current level of modern codification in the given countries; to identify the issues that arise in the process of codification of substantive and procedural tax law; to suggest ways to deal with them. Having studied the primary sources as well as national scholars' works on the issue of systematization of tax law, the author comes to the conclusion that despite the considerable amount of work on codification, to an extent the issue of 'legal uncertainty' is still there in each of the countries. In the author's opinion the given issue can be handled with the help of systematic codification of legal norms based on the following principles: *firstly,* to codify tax law it is necessary to provide due internal unity of the system of law and the system of legislation; *secondly*, in the course of codification of tax law, it should be viewed as an independent branch of law; *thirdly*, it is viable to regulate tax procedures by the norms of tax procedural law exclusively, to differentiate them from the norms of administrative process; *fourthly*, to unite the tax procedural norms into a consolidated legal act; and, *fifthly*, to assign the status of constitutional laws to the consolidated legal acts

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adopted in the process of codification of both norms of substantive and procedural tax law.

Keywords: Taxes; Tax Law; Tax Codification; Tax Code; Code of Tax Procedures; Codification of Tax Law; Legal Uncertainty; Crisis of the Sources of Law.

JEL Classification: K34; K40.

1 Introduction

On the basis of the analysis of legislation and law enforcement practice in the EU member countries (the Czech Republic, Poland) and non-EU post-Soviet countries (Russia, the Republic of Belarus) the author considers the role of codification of substantive and procedural law in terms of dealing with the issue of 'legal uncertainty' in the sphere of tax law and tax legislation.

The author sets the goal to determine the level of codification of tax law in the given countries; to identify the issues that arise in the course of codification of substantive and procedural tax law; to suggest ways to deal with them.

Taking into account the level of modern codification of tax law in different countries and the role of tax law in national legal systems, the author comes to a conclusion that the problem of ‚legal uncertainty' in the given area of law and legislation can be solved by means of systematic codification of tax law based on certain principles, namely: 1. To codify tax law it is necessary to provide due internal unity of the system of law and the system of legislation; 2. In the course of codification of norms of tax law, it should be viewed as an independent branch of law, which will allow one to minimize the number of references to the norms of other public branches of law; 3. It is viable to regulate tax procedures by the norms of tax procedural law exclusively and to differentiate them from the norms of administrative process. The author believes it should make the tax process clearer and more transparent both for taxpayers and for tax bodies; 4. For the sake of ease of application substantive norms of tax law should be collected in a consolidated legal act (e.g. a Code), and not in separate acts regulating particular taxes; 5. The consolidated legal acts adopted in the process

of codification of both norms of substantive and procedural tax law shall be assigned the status of constitutional laws.

At the same time the author comes to a conclusion that at present the codification of procedural tax norms (tax procedures) has been carried out most fully and thoroughly in the Czech Republic and in the Republic of Poland, and that other countries still have a lot of work to do to differentiate tax and administrative procedures. As for Russia, a lot of work has been done in terms of substantive tax law codification. The author also points out that all the countries should make a decision whether they will raise the status of codes to the level of constitutional laws.

The research is based on the legislative experience of the Czech Republic (Karfíková, 2015: 188–199), the Republic of Poland (Etel, 2016: 71–86, Popławski, 2016: 15–28), Russia (Chernikova, 2014: 80–84, Chernik, 1997: 4) and the Republic of Belarus (Abramchik, 2016: 29–50).

2 Brief characteristic of codification processes carried out in some EU member countries (as exemplified by the Czech Republic and the Republic of Poland) and post-Soviet non-EU countries (as exemplified by the Republic of Belarus and Russia)

Before highlighting the differences and similarities in the approach to tax law codification in the countries mentioned above, let us characterize the codification processes in the sphere of tax law that have already taken place there and their results.

2.1 Tax law codification as exemplified by the legislation of the Czech Republic and the peculiarities of the Tax Code (Tax Ordinance) of the Republic of Poland

2.1.1 History of codification of tax law in the Czech Republic

Just like in any other branch of law, from the viewpoint of functions of legal regulation and the interrelationship of legal norms, there is a substantive and a procedural part in tax law. Substantive tax law regulates rights and

obligations that arise as a result of establishment and collection of a particular tax. Procedural tax law regulates legal financial relations (subjective rights and obligations), the practical application of which is necessary when in order to achieve one's goal provided by the norms of material law one has to involve tax and financial bodies as public authorities.

In the Czech Republic legal regulation of particular taxes is contained in separate substantive acts regulating the establishment and collection of particular taxes. The given acts are not codified or consolidated into a single codified act in the Czech Republic.

As for the procedural tax law, its codification took place in the following way. In the period from 1953 to 1992 the procedural tax law of the Czech Republic was not codified, and the norms of procedural tax law were stipulated in the decrees of the Ministry of Finance, and not in legal acts.

As part of the tax reform related to the tax process in 1992 Act no. 337/1992 Sb. "On the administration of taxes and levies" (Zákon č. 337/1992 Sb., o správě daní a poplatků) was adopted, which applied to the regulation of the whole scope of issues related to tax procedures and contained 107 paragraphs. The adoption of the given law changed the concept that had existed before. Firstly, regulation of procedural tax law now was carried out at the level of law. Secondly, it was compliant with the traditional approaches applied in the developed countries of continental Europe, such as Germany (e.g. Abgabenordnung) and France (Code des procédures fiscales), where tax process and procedures are regulated by special codified acts and the autonomy of tax law, including its procedural part, is obvious. At the same time, the substance of procedural tax law could be contained in separate substantive legal acts regulating the establishment and collection of particular taxes as part of the taxation system. Act no. 337/1992 Coll. "On the administration of taxes and levies" stipulated the principle, according to which the provisions of the given Act are effective unless otherwise provided by an international agreement or tax legislation (substantive tax legislation, § 96–97). The provisions of § 99 of the Act no. 337/1992 Sb. "On the administration of taxes and levies" it is stated directly that Administrative procedural code (Zákon č. 71/1967 Sb. O správním řízení (správní řád) is not applied to tax procedures. Thus, by the tax Act no. 337/1992 Coll.,

"On the administration of taxes and levies" legal regulation was singled out as autonomous regulation of tax procedures independent of the administrative code.

The next step on the way to codification of procedural tax law in the Czech Republic was the adoption of a new act in 2009 – Procedural tax order (Zákon č. 280/2009 Sb., daňový řád). It contained 299 paragraphs and came into effect on 1 January 2011. As for the relations between the Procedural tax code ('daňový řád'**)** and the administrative procedural code ('správní řád'), the priniciple that had existed before was preserved and stipulated in § 262 of the new act: "The administrative procedural code shall not be applied to the administration of taxes". As for the application of tax procedural order (code) to the procedural norms contained in other substantive tax acts, § 4 of this Procedural tax order (code) points out that separate provisions of the procedural tax code shall be applied in case another act does not regulate the tax administration otherwise. Thus, after the new procedural tax order (code) came into effect, procedural norms of substantive law preserved their primacy, and were followed by the procedural norms enshrined in the procedural tax order (code).

When assessing the codification process in the sphere of tax law, one can agree with Prof. Karfikova (Karfíková, 2015: 188–199) pointing out we can speak of partial codification of tax legislation of the Czech Republic, and it is mainly related to the tax process. In 1992 they managed to replace the initial procedural act adopted in 1962 in the form of a decree with an independent, comprehensive regulation. And in 2009 a codified procedural tax act was adopted – the Procedural tax order (code). The adoption of this code (Zákon č. 280/2009 Sb., daňový řád) was a success and a result of years of work on the codification of procedural tax legislation carried out with the aim of dealing with the issue of 'legal uncertainty'. But since the procedural norms have been codified successfully, Czech scholars have still have to answer the question whether there should be an attempt to codify the norms of substantive law regulating the establishment and collection of particular taxes and to consolidate them in a single legal act (code).

2.1.2 History of codification of tax law of Poland

The codification process of tax law in Poland has many years of history. One can distinguish several stages in it.

According to Professor Etel (Etel, 2016: 71–86) in Poland general tax law was for the first time unified in the form of a single legal act in 1934. On 15 March 1934 Tax Ordinance Law **(**Ustawa z dnia 15 marca 1934 Ordynacja Podatkowa) was adopted, which partially codified tax law. It was one of the first legal acts of this kind in Europe. One should note here that the adopted "ordinance" according to the principles of legislative technique was equivalent to a "code". The Ordinance covered all the regulations regarding the operation of the taxation system (general tax law) except those regulating the establishment and collection of particular taxes. According to Professor Etel (Etel, 2016: 71–86) it is on example of partial codification of tax law.

The Tax Ordinance Law of 1934 regulated the most important institutions of general tax law in 212 Articles. It consisted of 5 parts: general provisions; tax assessment procedure; mandatory provisions; criminal law provisions; transitional and final provisions. It was a codified legal act of high level. The Tax Ordinance expired in 1946, as it did not fit the new reality of socialist economy after the World War Two.

According to Professor Etel (Etel, 2016: 71–86) since 1946 there began a process of general tax law de-codification. A number of Government decrees were implemented in 1946 on the following issues: 1) of 16 May 1946 On Tax Obligations (was replaced by the Decree of 27 October On Tax Obligations which was in force till the the implementation of the Act on Tax Obligations of 19 December 1980: 2) The Tax Procedure Decree of 16 May (expired in 1980, when the tax procedure was encompassed by the amended Code of Administrative Procedure); 3) Decree of 11 April 1947 on Fiscal Penal Law (was abrogated by the Fiscal Penal Law of 13 April 1960; later the norms of fiscal penal law were codified in the Act of 10 September 1999 – the Fiscal Penal Code).

Professor Etel (Etel, 2016: 71–86) points out that starting from 1 January 1998 general tax law in Poland has become codified again. It is due to the

adoption of the Act of 29 August 1997, which was called Tax Ordinance and came into force at the beginning of 1998 (Ustawa z dnia 29 sierpnia 1997 Dz.U., Ordynacja Podatkowa). According to Art.1, the given Act in 344 Articles shall regulate: tax obligations, tax information, tax proceedings, tax inspection and investigation activities, and fiscal secrecy. In fact, the scope of the Act is larger, which is clear from the titles of its sections. The Tax Ordinance is composed of 11 sections: I – General Provisions (Art. 1–12); II – Tax Authorities and Their Competence (Art. 13–20); III – Tax Obligations (Art. 21–119); IV – Tax Proceedings (Art. 120–271); V – Inspection Activities (Art. 272–280); VI – Tax Audit (Art. 281–292); VII – Fiscal Secrecy (Art. 293–305); VIIa – Exchange of Tax Information with Other States (Art. 305a–305o); VIII – Criminal Provisions (Art. 306 prescribes punishment for financial disclosure. The provisions that regulate financial crimes and offences more fully are part of the Fiscal Penal Code); VIIIa – Certificates (Art. 306a-306n), and Section IX – Amendments to the Provisions in Force, Transitional Provisions and Final Provisions (Art. 307–344).

According to Professor Etel (Etel, 2016: 71–86) and Doctor Poplawski (Poplawski, 2016: 15–28) the Tax Ordinance of 1997 is merely partial codification of tax legislation. Just like in the Czech Republic it lacks provisions of substantive tax law regulating the order of establishment and collection of individual taxes. They assume that the Tax Ordinance codifies only general tax law. However, it should be pointed out that the currently effective Ordinance lacks regulations traditionally classified as a general part of tax law, too.

2.2 Codification of tax legislation of Russia and tax codification in the Republic of Belarus

2.2.1 Codification of tax law and legislation in the Russian Federation

Highlighting the issue of codification of tax law and legislation in the Russian Federation it should first be noted that the structure of Russian tax legislation, as it is pointed out by Professor D. G.Chernik (Chernik, 1997: 4)

started forming as relatively coherent – compared to the Soviet period of 1990–1991 – only in 1992. It is also noted by Professor E. V. Chernikova (Chernikova, 2014: 80–84) that the legal framework of taxation in the Russian Federation was laid only in 1992 with the adoption of a whole range of acts regulating individual taxes and the Act no. 2118-1 of 27. 12. 1991 "On the Principles of Taxation System in Russia".

In the period from 1992 to 1998, the system of legal regulation of substantive and procedural tax law was the following. The core was Act no. 2118-1 of 27. 12. 1991 "On the Principles of Taxation System in Russia". The given act contained the most significant concepts and principles of taxation system, its structure, kinds of taxes, taxpayers' obligations, etc. At the same time at the federal and regional levels a whole set of substantive acts was adopted to regulate the establishment and collection of particular taxes. There was also Act no. 943-1 of 21. 3. 1991 "On the Tax Authorities of Russia" in accordance with which there appeared a State Tax Service (Federal Tax Service today), which was part of the Ministry of Finance of Russia for some time, as well as the rights and obligations of the tax service were determined. The norms of tax law were also regulated by the decrees and other regulatory acts of the Government of Russia. Besides, tax norms were often part of non-tax acts adopted in other branches of law, e.g. such acts as "On the Militia", "On the Education" or "On the Firefighting Service" and were related to tax benefits. The Tax Service could also issue their regulatory acts related to taxation. In 1992 act "On the Principles of Taxation System of Russia" provided for 47 taxes and levies (19 at the federal level, 5 at the regional and 23 at the local level), as well as 7 obligatory payments to non-budget social funds. After 1993 there were 2 more federal taxes and 130 to 300 regional and local ones. By the end of 1998, 63 taxes and levies (56 taxes and 7 contributions to social funds) were charged. As it is pointed out by Professor E. V. Chernikova (Chernikova, 2014: 80–84) by the end of this period legal regulation of tax relations was characterized by lack of stability and clarity and frequent changes in the rules of the 'game with the State', which predetermined the adoption of the Tax Code of the Russian Federation in 1998 as a codified legal act.

By 1998 tax law and tax legislation needed systematization. The form that was selected for the systematization of tax legislation of Russia was codification. In the Russian Federation the object of codification of legislation is formed based on the results of dividing the legal system into branches. The systematization of legislation regulating public finance was codified at the sub-branch level, so the codification of Russian tax legislation went along the same, sub-branch way. The result of the codification was the adoption of the Tax Code of Russia in 1998. The Tax Code was adopted in two parts named Part 1 and Part 2. The first part of the Tax Code of Russia was adopted in 1998, the second one was adopted in 2000. According to Russian scholars S. G. Pepelyaev (Pepelyaev, 2000: 496) the Tax Code of the Russian Federation can be referred to general tax codes.[2] But despite this fact, it lacks codification of procedural norms regulating the tax process and tax procedures. For this reason Professor Chernikova (Chernikova, 2014: 80–84) writes that the Tax Code of Russia contains almost no procedural norms regulating the relations between tax bodies and taxpayers, which causes disputes for both sides. The absence of legal regulation of tax procedures is a serious issue in the Russian tax legislation. The concept of "tax administration" which is actively used in the Czech Republic, Poland and the Republic of Kazakhstan (the third special part of the tax code of the Republic of Kazakhstan is devoted to tax administration) is not present in the Russian legislative lexicon.

The structure of the Tax Code of the Russian Federation. The Tax Code of Russia consists of Part 1 and Part 2. The first part of the Tax Code is considered to be general, and it encompasses the norms regulating the principles of tax regulation in the state; part two is considered to be special and it stipulates the provisions that determine the establishment and collection

2 Depending on the object of regulation there are general and special tax codes. General tax codes contain substantive and procedural norms regulating taxation on the whole. Such codes regulate the principles of tax collection, the taxpayers rights and obligations, the strucure and the legal status of tax bodies, the procedures of tax calculations and payment, control over the accuracy of tax calculations and the timeliness of their payment, appeal of actions and decisions of tax bodies and their officials, responsibility for tax legislation offences. Special tax codes regulate particular kinds of fiscal payments. For example, in Algeria there are several codes of this kind: the Code of direct taxes and related payments; the Code of taxes on sales; the Code of registration duties; and the Code of stamp duties. In Belgium there is a Code of inhabitant taxes.

of particular taxes and levies that make up the taxation system (system of taxes and levies) of the given tax. The Tax Code consists of sections divided into chapters, which are divided into articles. Part One of the Tax Code of the Russian Federation consists of 7 sections that regulate the relations making up the basis for the whole taxation system. Sections contain chapters (20 chapters), and chapters contain articles (142 articles). Section I, "General provisions", encompasses the principles of taxation, the sources of legal norms on taxes and levies, the key concepts, the system of taxes and levies. Section II is devoted to the rights and obligations of the participatns of tax relations – taxpayers and tax agents, as well as their representatives. Section III highlights the basics of the legal status of tax and customs bodies and the tax police. Section IV is the biggest: it contains 6 chapters and establishes general rules of the performance of tax obligations. Section V is devoted to tax reporting and tax control. Section VI identifies kinds of tax offences and the responsibility for committing them. Section VII regulates appeals against the actions of tax bodies and authorities. Part Two of the Tax Code of the Russian Federation has 4 sections, 31 chapters and 398 articles. In terms of content it is a special part, as it regulates federal, regional and local taxes and levies, their particular types and tax regimes.

The structure of tax legislation of the Russian Federation. Russian tax law and tax legislation codification was aimed at the reinforcement of the systemic character of legal acts, their unity and coherence. So it was important to develop the concept of "tax legislation" and to establish the correlation between the tax code and the acts of tax legislation, as well as other sources of tax law. In the Tax Code of Russia the concept of "tax legislation" is named "the tax and levy legislation". The tax code occupies the key role in the pyramid that forms the structure of the "tax and levy legislation of Russia"; its branch-forming role and primacy among other acts making up the "tax and levy legislation" is fixed. The second place in this pyramid belongs to tax laws. It is stipulated in the Tax Code of Russia that an act on taxes and levies is always a law.

The federative framework of the Russian Federation has left its mark on the structure of the legislation regulating the establishment and collection of taxes. Art. 1 of the Tax Code of Russia stipulates the three-level

structure of the tax and levy legislation: 1) federal level ("tax and levy legislation of the Russian Federation") – the Tax Code of Russia and the federal laws adopted in accordance with it (federal acts that amend the Tax Code of Russia, operational acts, etc.); 2) regional level ("tax and levy legislation of constituents of constituent entities of the Russian Federation") – tax laws of the constituent entities of the Russian Federation adopted in accordance with the Tax Code of Russia; 3) local level ("municipalities' regulatory acts of on taxes and levies") – municipal legal acts on taxes and levies adopted by the representative bodies of municipalities in accordance with the Tax Code of the Russian Federation.

Tax legislation is defined not only by means of establishing its structure and content, but also via determining the borders of the tax code with other sources of tax law. The legislator established the primacy of the Constitution over the Tax Code. In accordance with the Constitution the prevalent power of a ratified international agreement has been established in case there is a collision between the Tax Code and an international treaty in the course of regulation of tax relations. (p. 1 Art. 7 of the Tax Code of Russia). The correlation of the Tax Code and bylaws adopted for the regulation of tax relations is quite obvious: a bylaw shall correspond to the law to provide for the full observation of the principle of legality.

2.2.2 Codification of tax law and legislation in the Republic of Belarus

The means of regulating tax relations in the Republic of Belarus in the period from 1991 to 2001 (i.e. before the creation of a codified legal act in the sphere of tax law, which was the Tax Code of the Republic of Belarus, adopted in 2002) is in many ways similar to the Russian version. Doctor Abramchik (Abramchik, 2016: 29–50) points out that during this period the provisions of the general part of tax law were encompassed in the Act "On Taxes and Fees Raised in the Budget of the Republic of Belarus". The given law regulated the general issues related to the all-state obligatory payments; determined the legal status of taxpayers and tax bodies; contained the kinds of tax offences and responsibility for committing them. It characterized tax control and the order of appealing against authorities and state bodies'

actions and decisions. The norms of a special part of tax law were enshrined in the acts "On a Value Added Tax", "On Excises" and "On an Income and Profit Tax", "On an Individual Income Tax", "On a Real Estate Tax", "On Payments for Land", "On Natural Resources Use Tax (ecological tax"), Art.1335/1991), "On a Fuel Tax", etc. At that time tax relations were regulated by the decrees of the President of the Republic of Belarus and of the government. According to Doctor Abramchik (Abramchik, 2016: 29–50) for 10 years tax legislation developed dramatically. A large number of tax Laws, Decrees and Edicts of the President of the Republic of Belarus, Decrees of the Council of Ministers of the Republic of Belarus made it difficult to use and apply it both for the taxpayer and the tax bodies. For this reason there appeared an overdue need to systematize tax legislation of the Republic of Belarus. With the Decree of the President of the Republic of Belarus of 10 April 2002 no. 205 the Concept of improvement of the legislation of the Republic of Belarus which named codification to be the key development path for the system of legislation allowing to achieve a single, legally coherent regulation in the branches and certain institutes of law. For this reason, codification was selected as a means of its systematization.

It should be noted here that in the Republic of Belarus there is a legal definition of codification. Thus, Art. 1 of the Law of the Republic of Belarus of 10 January 2000 N 361-3 "On the Regulatory Legal Acts of the Republic of Belarus" defines codification as "a kind of systematization of regulatory legal acts accompanied by the procession of the legal content they provide by means of uniting regulatory acts into a single legal act that contains a systematized account of legal provisions aimed at the regulation of a particular area of public relations". Article 2 of the given Law defines a codified act as "an act providing for comprehensive systemic regulation of a certain area of public relations".

The systematization of legislation in the Republic of Belarus opted for the codification at the sub-branch level (creation of budgetary, tax, monetary laws), so the Tax Code of the Republic of Belarus is of a branch character. It refers to general tax codes.

Just like in Russia, in the Republic of Belarus the Tax Code was adopted in two parts. In the Republic of Belarus they are called General and Special

Parts. The General Part of the Tax Code was adopted at the end of 2002 and was put into effect since 1 January 2004 with the exception of separate provisions that came into effect on the day the Special Part of the Tax Code was put into effect. The Special Part was adopted at the end of 2009 and came into effect on 1 January 2010. The General Part of the Code encompasses the norms regulating the principles of tax regulation in the given state, and the Special Part covers the provisions that determine the collection of particular taxes and levies that together make up the taxation system (tax and levy system) of the Republic of Belarus.

The method of structuring a codified text in the Republic of Belarus is similar to that in Russia: a part – a section – a chapter – an article. The peculiarity of the structure of the Tax Code of the Republic of Belarus is the presence of notes and addendums. The addendums usually contina individual taxes rates (addendum 1 – excise tax rates; addendum 2 – land tax rates, etc.) Overall there are 25 addendums in the Tax Code of the Republic of Belarus that make up a unified whole with the legislative text. The note is at the very beginning of the text of the Code. It covers the peculiarities of making references to the Code in case it amended. The note was introduced to the Tax Code by Act N 174-3 of 15 October 2010.

The General Part of the Tax Code of the Republic of Belarus consists of 4 sections*:* Section 1. "General provisions"; Section 2. "Tax obligations"; Section 3. "Tax accounting and tax control"; Section 4. "Tax and customs authorities of the Republic of Belarus. Appeal of decisions of tax authorities". The given sections contain 11 chapters: chapter 1 "Basic provisions"; chapter 2 "Payers of taxes, levies and fees"; chapter 3 "Objects of taxation"; chapter 4 "Tax obligations"; chapter 5 "Ways of ensuring the execution of tax obligations, payment of penalty fees"; chapter 6 "Compulsory execution of tax obligations"; chapter 7 "Offset, tax refund"; chapter 8 "Tax accounting. Tax declaration"; chapter 9 "Tax control"; chapter 10 "Tax and customs authorities of the Republic of Belarus"; chapter 11 "Order and terms of appeal of decisions of tax bodies and their officials' action (inaction)".

The Special Part of the Tax Code of the Republic of Belarus encompasses the order of application of all republican and local taxes, levies (fees) as well as special taxation regimes. It establishes all the necessary elements of a legal

framework of each tax: structure of payers, objects of taxation, tax base, tax rates, list of tax benefits, as well as the order of calculation and collection of taxes, levies and fees, the terms of their payment and of reporting the sums that are subject to payment to the tax bodies.

The Tax Code of the Republic of Belarus contains a definition of "tax legislation", enshrines the branch-forming function of the tax code and establishes the primacy of the tax code over any other legal norms regulating tax relations.

In contrast to the Russian Federation, the Republic of Belarus is a unitary state and has a 'monolithic' tax legislation, which is a single regulatory body, a totality of regulatory acts (or acts of tax legislation) adopted in accordance with the tax code in order to regulate tax relations. This kind of approach to legislation means that all other acts of tax legislation are secondary to the tax code and cannot contradict it. Thus p. 2 Article 2 of the Tax Code of the Republic of Belarus provides: "Provisions of legal acts adopted on the basis and in pursuance of the given Code cannot contradict the provisions of the Code or exceed the content of the given provisions or the authority that they provide to a body". Secondly, this legislative approach implies that legislative acts in this kind of legal interpretation may not only be laws, but also bylaws.

All possible forms of legal acts of tax legislation are listed in the Tax Code of the Republic of Belarus. Art. 2 of the Tax Code contains the following definition of tax legislation: "The Tax Code of the Republic of Belarus is a system of legal regulatory acts adopted on the basis and in accordance with the Constitution of the Republic, which includes: the given Code and acts adopted in accordance with it that regulate tax issues; President's decrees, edicts and orders; regulatory acts adopted by the republican administrative bodies, local government and self-government bodies, regulating tax issues and issues on the occasions and within the frame provided by the given Code, as well as tax acts adopted in accordance with it, Presidential acts and decrees of the Government of the Republic of Belarus".

We should note here that such an extended approach to the definition of tax legislation implying that not only laws but also bylaws refer to the tax legislation does not comply with the approach determined in the Tax Code

of the Russian Federation, in accordance with which an act on taxes and levies is always a law.

The Tax Code of the Republic of Belarus prohibits inclusion of tax norms into 'non-tax' legal acts. Thus, according to part 2 p .1 Art. 3 of the Tax Code of the Republic of Belarus "inclusion of provisions regulating tax issues into other acts of legislation is prohibited unless provided otherwise by the given Code or by the President of the Republic of Belarus". This kind of legislator's approach is aimed at the exclusion of any collisions between lex generalis and lex specialis in the regulation of tax relations. By establishing the rule by which a tax norm can be part of tax legislation only, the legislator in this way gives an order to the enforcers of law (in the administrative and judicial spheres) to apply only the norms of tax legislation (lex specialis) to resolve tax disputes.

The Tax Code of the Republic of Belarus also prohibits the application of tax legislation on the basis of analogy (e.g. p.7 Art. 3 of the Tax Code of the Republic of Belarus).

Just like in Russia the legislator establishes the primacy of the Constitution of the Republic of Belarus over the tax code. In case of any collision between the tax code and an international treaty in the regulation of tax relations, Article 5 of the Tax Code of the Republic of Belarus establishes the primacy of a ratified international treaty.

The correlation of a tax code and bylaws adopted for the regulation of tax relations is quite specific in the Republic of Belarus. Thus, President's decrees occupy a special place in the system of legal acts of the Republic of Belarus as legal acts of the head of the state that have the force of law and are issued in accordance with the Constitution on the basis of legislative authorities that the Parliament delegated to him, or in case of emergencey (a temporary decree), in order to regulate more important public relations (Art. 2 of the Act "On the Regulatory Legal Acts of the Republic of Belarus"). In case of any collision between a tax norm from the President's act and an act from the tax legislation the primacy in some cases may be given to the President's acts.

It may happen by force of p.2 Art.3 of the Tax Code of the Republic of Belarus: "*The provisions of regulatory legal acts adopted on the basis and in pursuance of the given Code cannot contradict the provisions of the given Code or exceed the framework of its content or the authorities provided to a relevant body. The provisions of the given point do not apply to the acts of the President of the Republic of Belarus*". A similar norm can be found in p. 4 Art.3 of the Tax Code of the Republic of Belarus: "*In case of contradiction between the President's decree and the given Code or another law regulating tax issues, the given Code and another law are prevalent only in case the authority to issue a decree was given by law*". In other words, in the regulation of tax relations Presidential acts issued in accordance with the Constitution of the Republic of Belarus may be superior to the force of law, including the tax code.

3 Similarities and differences in the approach to tax law codification

As we can see certain approaches and concepts were used in the course of tax law codification in each country. These approaches and concepts have both similarities and differences.

Speaking of similarities, first of all one should point out the common approach to the concept of 'codification' in the theory of law in the given countries. By codification one means single, systemic, legitimate regulation of a certain area of legal relations. Codification is firstly legislative activity aimed at the creation of single systematized collection of legal provisions. The work on codification usually starts when due to the amount and variety of legal provisions the existing legal regulation is hard to comprehend.

The second similarity is that in the national systems of law tax law is either an autonomous branch of law or a subbranch of financial law. Such a position causes similarity in the approach to the codification of tax relations. They are viewed as independent public relations, and tax law is viewed as an independent public branch of law. It is particularly obvious in the case of tax order (code), regulating the issues in tax process and procedures

adopted in the Czech Republic.[3] It's pointed out clearly in the given law that tax procedures are regulated only by the norms of tax law, and provisions of the administrative procedural law shall not be applied.

The third similarity is that in none of the countries under consideration the consolidated codified tax laws have not been assigned the status of constitutional laws.

The fourth similarity is that despite quite extensive codification work carried out in the given countries in the sphere of tax legislation, the issue of ‚legal uncertainty' is still pressing both for the norms of substantive and procedural tax law.

Speaking of the differences we should note one significant here. This difference is related to the approach to the codification of procedural and substantive norms of tax law and tax legislation. Thus, for example, in the Czech Republic and in Poland there is a separate single codified act, which regulates the tax process and procedures. In Russia and in the Republic of Belarus there is no such codified act.

4 Conclusion

Artavanis et al. (2016) concluded that contemplates the importance of institutions and political willpower for the persistence of tax evasion. Having characterized the codification processes and having identified the key similarities and differences in the approach to the codification of tax law one can make the following conclusions. Despite rather a extensive codification work carried out in this field the issue of "legal uncertainty" is still present in the given countries both in terms of substantive and procedural tax law. According to the authoer the issue can be solved by means of a systemic codification of tax norms provided the following principles are observed: 1. To codify tax law it is necessary to provide due internal unity of the system of law and the system of legislation; 2. In the course

3 In the provisions of § 99 Act 337/1992 (O správě daní a poplatků) it was pointed out directly that the administrative procedrual code (Zákon č. 71/1967 ze dne 29. června 1967 o správním řízení (správní řád) shall not be applied to tax procedures. Thus, legal regulation by the tax law (Zákon č. 337/1992 Sb., o správě daní a poplatků) was made independent of the administrative order (code).

of codification of norms of tax law, it should be viewed as an independent branch of law, which will allow one to minimize the number of references to the norms of other public branches of law; 3. It is viable to regulate tax procedures by the norms of tax procedural law exclusively and to differentiate them from the norms of administrative process. The author believes it should make the tax process clearer and more transparent both for taxpayers and for tax bodies; 4. For the sake of ease of application substantive norms of tax law should be collected in a consolidated legal act (e.g. a Code), and not in separate acts regulating particular taxes; 5. The consolidated legal acts adopted in the process of codification of both norms of substantive and procedural tax law shall be assigned the status of constitutional laws.

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Tax Fraude in French Law – Selcted Issues

Mariola Lemonnier[1]

Abstract

This article deals with the tax fraud in France from juridical and theoretical point of view. The main aim of this contribution is to confirm, that the legal problems of the law of tax fraud in France revolve around issues, that are discussed in many legal systems. This article draws attention to the characteristics of good faith in French law and the approach to tackling tax fraud and its legal analysis.

Keywords: Tax; Fraud; French Law; Good Faith; Fiscal Law.

JEL Classification: K34.

1 Introduction

This article discusses the problematics of French law, referring to tax fraud problems, occurring also in many countries.

Article points to the contribution of French legal doctrine, to the understanding of jurisprudence of European courts, and to a better understanding of such a broad and long-developed theory of tax fraude.

The concept of good faith is also discussed in the article, the function of good faith in the relations between the taxpayer and the tax authority is crucial. The article shows not only comparable aspects in the matter of tax fraude but also some tax law considerations developed in French law, which can be an example for other countries, such as the theory of normal management (gestion normale de l'entreprise).

The method used in this article is the method of analyzing the legal regulations (dogmatic method) and combines elements of civil, penal and tax law.

The problem presented in this article shall be perceived as important and actual. Tax fraud constitutes the deficit from 60 to 80 billion euros per year for the French Treasury. This amount seems very small when compared

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to the amount to tax evasion around the world (Tax Fraud Committee, Annual report 2015).

Fraud applies to actions of both individuals and businesses. It shall be emphasized that VAT, especially in the EU, is one of the most important parts of budget. In fact, when we look at the tax revenues of the state, VAT remains it's main pillory. It represents almost 50 % of annual tax revenues in France(http://www.vie-publique.fr/decouverteinstitutions). Every state including France, is interested in preserving it's income and protecting itself against fraudulent activity of operation which can also facilitate fraud.

2 The elements of tax fraud in French law

Tax is an instrument in the legal system (Mrkývka, Czapski, 2017: 53), instrument of the company management

(Gajewski, 2017: 366) and an element of the state's economic policy (Dubut, 2017: 123). Under French law, a tax fraud (fraude fiscale) has no legal definition (Martinez, 1984: 10). It is generally regarded as an act commited in bad faith (Mortimer, 2003: 904), against the law, and also harmful to the rights of others. The French tax administration's view of illegal activities lacks the definition of tax fraud and is based on the lack of good faith. The presumption of being a good faithful taxpayer in France became an essential element of the tax-law relationship.

Good faith, of taxpayer in France, results from mutual loyalty (administration and taxpayer).

3 Good faith of the French taxpayer

Recognition of a good taxpayer's faith in France – as an additional guarantee in a tax procedure – is being treated as the right of a taxpayer, who is entitled to use it. The function of good faith in the relations between the taxpayer and the tax authority is very important. It is accompanied by a long process based on dialogue and partnership, on information provided by the taxpayer but not on false facts relevant to tax fraud. In the case of bad faith, the reaction of the French tax administration is adequate. A taxpayer who is aware and acts with the intention of tax evasion, will not avoid

sanctions. Tax fraud occur in many forms, of which the traditional ones are defined in the General Tax Code, which also provide the relevant criminal penalties. At the same time, the taxpayer is free to manage the undertaking in accordance with the principles of entrepreneurship. Part of the French doctrine believes that the issue of good faith in the tax procedure is not secured by the provisions of the General Tax Code, but it is a tool on which the issues of punishing fraud and simulated activities are based.

The French judge and tax administration tries to attach to this – undoubtedly subjective aspect of the taxpayer's activity – an aspect of a moral and ethical nature, bur from this releve not an immediate tax obligation (obligation fiscale). In the procedural sense, the above does not stand for theevidence, but rather for the tax administration's interpretation of the facts. The jurisdiction allows the tax authorities to link the taxpayer's good faith to his real situation.

4 Good faith in French law

In a dictionary, developed by the French Association, Henri Capitant entitled – Dictionary of Legal Concepts of the Henri Capitant Association (Cornu, 2016, bonne foi), the authors point the duality of the concept of good faith. Good faith, on the one hand, is a misconception about the existence of a legal situation in accordance with the law, while on the other hand means loyal behavior (or at least behavior perceived as normal for given circumstances), which in particular requires the due dilligence. This is the attitude of an honest man. At the Henri Capitant congress held in Louisiana in 1992 (Bénabent, Rapport français, 1994: 291–293), a homogeneous and uniform definition of the concept was not presented**.** Concluding congress in Luisiana prof. I. Loussouarn confirmed that the concept of good faith concerns less law and rather psychology and morality (Association Henri Capitant, 1994). Good faith is an important philosophical category, which underlies many legal institutions; but it can not be considered as an institution itself. At the Congress, prof. Gorphe proposed to give up the concept of one legal definition of good faith, but rather perceive it as a principal for the judge applying the law. In the same sense, prof. G. Ripert combined

the notion of good faith with more general idea of morality (Association Henri Capitant, 1994).

It is normal to conclude the good faith from the concept of contract or the obligation of loyalty. It is precisely on the basis of this very vague conception of good faith, that the French jurisdiction, confirmed by doctrine, extended the scope of the concept of good faith and thereby made it become like a "sea without coast" «mer sans rivage". The purpose of this extension was to protect the economically weaker party in the creation and implementation of the contract. The concept of good faith remains too moral and has too vague framework to produce a direct effect in almost any positive terms. He also noted that it's the essential function is to explain the moralization of contractual relations between contractors, the number of which is growing both through the fragmentation of protection laws but also through French jurisdiction on mitigating the imbalance between the parties in the contracts. Although the concept of good faith serves the general purpose of moralizing (moralizing) the law, it is, on the other hand, unsuitable for assessing the inequality of economic power between the parties. By using this faith for this purpose, the jurisprudence changes content of this concept, causing the loss of all coherence and unity of understanding.

The contemporary extension of good faith on the entire rights of obligations, in order to sanction the abuse of economic power and restore balance, is unnecessary and unjustifiable -according to some authors Prof. Carbonnier emphasized that "Excess can destroy a good idea" *« L'outrance peut perdre une idée juste »*

(Carbonnier, 1994: 113). Being in a good faith means the existence of the lawful legal event, while the reality is different. In such a case, the law comes to the benefit of an entity that is in good faith, despite the irregularities in its real situation.

The traditional approach to good faith is found in most countries and concerns a state in which there is a misconception of reality in the long term. On the one hand, good faith is ignorance of something that someone should know. In another approach, good faith is the right opinion and the firm belief that the possessor, for example, has acquired the property. This is a legal unknowing, that is a complete belief of the buyer that, for

example, the possesor has the right to property and it is also a belief resulting from ignorance.

Good faith in such a relationship is analyzed in relation to the party which assert their rights and not depend on the actions of the other party. It is not necessary to prove that the other party is in bad faith. According to others, good faith is a belief based on erroneous premises of action or legal event, based on ignorance of irregularities – then it is a purely psychological concept, not a moral one. Therefore, it does not affect the existence (or it's lack) of good faith – the belief in the existence of a defect that does not exist in such a reality.

Misconception is the dominant element in the subjective concept of good faith – there is no moral connotation in such a good faith. The morality and social values determine the misperception of reality then has legal consequences.

Even if one traditionally approaches good faith, as an idea of erroneous belief, it is closely related to the state of mind of the subject, but it can not be analyzed only in terms of the psychological aspect. Despite the lack of positive law provisions in this regard, it is recognized that in order to obtain a legal effect, the error must be credible, justified. If it is not, despite good faith, the behavior of the person is therefore assessed negatively.

In simple terms, good faith is honest and loyal behavior. Honest behavior is inextricably linked to the intention of the subject, while loyalty can be understood as meaning to act in compliance with the standards and standards required in a given situation. Loyalty is adequate to good faith, but from legal point of view taxpayer good faith should stay in accordance with the objective morality and judge's morality. From this perspective, the element of intent gives way to the external criterion, which is analyzed according to social standards, not only subjective ones, which were recognized. There is an objective good faith when we examine the individual's behavior towards the norm, the standard, and not its true intention. However, the psychological element still plays a role in the analysis of this aspect of good faith.

As for VAT (TVA – taxe sur la valeur ajoutée), the French Council of State decided in the 1970s, that good faith could be treated as a basis for deduction, even for a false invoice issued by another dishonest entity participating in a VAT carousel – even if the legal provision applied to this situation provided for the prohibition of such a deduction (Council of State, 29 December 1978, Req. Nr 9405). This solution was taken over by the famous judgment of 12 January 2006 (The Court of Justice of the European Union, 12 January 2006, Aff. C-354/03).

5 Material and procedural elements of tax fraud in France

The beginning of the procedure related to tax fraud in French law may indicate the concurrence of criminal and tax law. The participation of the Tax Crimes Commission in the procedure avoids many confusions. The lawsuit in the case of tax fraud is filed by the tax administration. Tax Crimes Commission is participating in this procedure is an opinion-giving, yet fundamental and is being treated as an institution securing the taxpayer's rights. The legitimacy of the tax authority to initiate a criminal trial is an exception to the prosecutor's jurisdiction.

(Reki, 1995: 153). In general, in the process of tax fraud, the prosecutor is not the entity that can start the case. The tax administration files a lawsuit pursuant to art. 385 of the French Penal Procedure Code. The authority may also establish a civil party in such a process pursuant to Article L323 of the General Tax Code. A crime of tax fraud can occur in the case of base money laundering under Article 344-1 of the French Penal Code, and then it is an offense, that is autonomously qualified before a criminal court and the prosecutor's role in the initiation is substantial.

The lack of a positive opinion of the Commission in the matter means, that the tax authority will not be able to bring a case in tax-fiscal mode, but is required to be established as the civil part in the procedure. The initiation of a procedure against a taxpayer in a tax fraud case depends on the tax administration and administration has the power to initiate the procedure (Council of State, 5 November 1981, Gaillard, Req. 16212).

Only the legal base mentioned in the General Tax Code (fiscal law) is the basis for initiating the procedure against the fiscal fraud and also fiscal administration must prove from art. 1741, that bad faith of the taxpayer and other elements of fraud have occured. The proper informations are collected by the tax administration. In this sense, the administration assumes the role of a "policeman" based on the theory of normal management (gestion normale de l'entreprise). The theory developed on the basis of administrative jurisdiction of the Council of State indicates that from operation of a taxpayer qualified as an "anormal management act" (Cozian, 1999: 98), results a loss or costs to the entrepreneur without justification by the interest of the company (Council of State, 27 July 1984, SA Renfort Sevice, Req. n. 34588).

Another legal structure being referred to the tax fraud is the conception of the « abuse of law »- (abus de droit) and its application in tax law. This concept is based on the jurisdiction of the Court of Cassation and the Council of State and it indicates the sanctioning the fictitious taxschemes or actions of the taxpayer, which are aimed only to achieve tax purposes (Fouquet, 2006: 1999). Abuse of tax law was included in art. 64 of the General Tax Code, although there was a major discussion about the constitutionality of art. 64 with the taxpayer's rights as an individual right. The Council of State in this matter indicated that the Constitution protects freedom, but not to the same extent, depending on the place in the legal system also with regard to the juridicals norms. (Drago, 1991: 265).

The Constitutional Council leaves from in the theory of application of criminal law only by criminal courts, by the theory of juridical norm containing a criminal sanction. (Constitutional Council, 17 January 1989, n. 88–248). On this basis, the administrative judiciary uses the criminal law technique in cases of tax fraud (Constitutional Council, 2–4 March 2004, n. 2004–492DC).

If the basis of tax fraud qualification is the mechanism of abuse of the law, all transactions contrary to the will of the legislator are sanctioned. Also, not only transactions relating only to the tax purpose and also to the subjective approach of the action contrary to the ratio legis of the tax legislator are being prosecuted.

Carousel fraud is not only a fight conducted by national authority but also by the European Union, on the basis of VAT regulations. Both OLAF and Fiscalis, with european strategies stress the need to fight VAT frauds. In addition, in France and in Poland, there was established a connection between fraud and the need to exchange information and measures against tax havens (they are called countries refusing to comply with international standards- pays non conformes aux standards internationaux). Since 2009, France has signed bilateral agreements on exchanging mutual information about taxpayers, also aimed at repealing banking secrecy.

The Court of Justice of the EU dealt with fraud and pointed out the three elements indicating the abuse of tax law.(CJEC, 14 December 2000, C-110/99, REC. 2000.S.I-11569). First, there is an indication of non-compliance with the regulation motive, secondly they are abusive practices with the will to receive a tax advantage and create fictitious conditions for their receipt, and thirdly, the need for an individual assessment is indicated.

The taxpayer who has to show to administration that he could not see the fraud, should prove that he had a reasonable ignorance (ignorance légitime) about the fraud which exempt from liability. (Council of State, 1 July 2009, SARL Alain Palanchon, req. n. 295689). The Council of State indicates, that repetitive high-value deliveries for persons who did not conduct real operations are not acts in good faith, as well as supplies for an entity neither being enclosed in the National Register, nor being a VAT taxpayer, are similarly qualified.

French law treats the intentions of the taxpayer as fundamental and does not exempt from it any ideological (moral) arguments, state of depression or accounting errors caused by a financial disaster in the company, that underlies the personal problems of the company's managers.

Tax fraud should not be analyzed as a phenomenon of defense from tax, but rather asn an attitude towards taxes, that changes in French society depending on the state of the economy, the state of social peace, war or systemic changes. For example, after the French Revolution, paying taxes was treated as an honorary obligation. Yet it also has to be reminded, that in general the taxpayer wants to remove tax – as is a burden – and make it more bearable for him.

Tax fraud is sanctioned in French law the same way, as it is in Polish tax law and criminal law. Article 1729 of the French General Tax Code sanctions illegal activities, and Article 1741 of the Code indicates criminal penalties for tax fraude – as follows:

Without prejudice to the specific provisions laid down in this codification, any person who has fraudulently avoided or attempted to avoid payment of the tax in whole or in part, taxes referred to in that code, or voluntarily failed to make a declaration within the prescribed period, or voluntarily concealed the whole whether a part of the taxable amount, or insolvency or other fraudulent means in the collection of tax, or acted in a different manner, regardless of the applicable tax penalties of 500 000 euros and imprisonment for five years. The penalty is increased to 2 000 000 euros and up to seven years imprisonment if facts were committed in an organized criminal group or carried out or facilitated by means of: accounts opened abroad or contracts with foreign entities, through intermediation of individuals or legal persons or any authority, trust or comparable institution, or the use of a false identity or false documents within the meaning of art. 441-1 of the Criminal Code, or any other falsyfication, or a false tax residence abroad, either a fictitious act or having artificial or fictitious person.

The articles applies if the penality exceeds one tenth of the tax base or the amount of 153 euros. Everyone may be deprived of civil and family rights in accordance with the provisions of Articles 131-26 and 131-26-1 of the French Penal Code. The court may also order the publication of the announced decision and its distribution under the conditions provided for in Articles 131-35 or 131-39 of the French Penal Code.

The general tax fraud can be characterized by two relatively similar procedures with it's specific traits. General regulations allow the tax administration to investigate various situations. In fact, tax fraud is often very difficult to prove and unfortunately the lack of financial resources in the French budget negatively influences the assessment of the phenomenon of fraud, as well as the amounts whicha are actually being recovered by the tax authorities.

General fraud is regulated by the French Penal Code in Article 313-1. This is the question about using false personal data, using fraudulent methods,

to deceive another physical or legal person to the detriment of that person or a third party. The subject of fraud is the provision of services, transfers of funds, values or things, as well as actions to release or impose obligations on other person. Furthermore, the criminality of acts has been strengthened with the changes, of applicable sanctions and new legal acts, and in particular by the adoption in France of the law on combating tax evasion and serious economic and financial crimes.

To characterize the general tax evasion crime in Article 1741 of the General Tax Code, it is necessary to express the will to not pay the tax. As in a criminal case, the burden of proving the element of intenstion rmains within tax administration, as provided in art. L 227 of the Fiscal Procedure Code. If it has not been proven that the taxpayer knew that he had committed a fraud, then the act cannot be qualified.

According to settled French jurisprudence, if the voluntary nature of the proceedings is one of the basic conditions characterizing the tax evasion offense, it is also a sufficient condition. Therefore, if the voluntary nature of the acts is proved, it will not be necessary to prove that the taxpayer has appealed to unfair maneuvers, because they are specified in art. 1729 of General Tax Code or in Article 313-1 of the Criminal Code. General Code related frauds correspond to "inaccuracies" or "omissions" noted in a declaration or act indicating the elements to be retained for the tax base or amortization, as well as the restitution of a tax claim whose was incorrectly obtained.

In 2000, many Anglo-Saxon countries launched programs of the so-called "fiscal discipline", introducing an innovative approach to the relationship between tax administration and taxpayers (Gutman, 2008: 23).

France has also adopted this type of relationship. The program was based on a logical contrast between the interests of the administration and the taxpayer, and some countries introduced a cooperation mechanism, developing information exchange system. These mechanisms not only help to promote legal certainty, but also facilitate – sometimes strained – relations between the administration and the taxpayer.

6 Conclusion

Tax fraud is an institution that manage with the theory of civil, criminal and fiscal law. The complexity of the issues explain interest to the topic. The article may be a contribution to discussions in other countries on such a multidimensional coverage. It is known that a taxpayer's bad faith determines the nature of his liability. Good faith on the one hand is a misconception about the existence of a legal situation in accordance with the law, in the second approach means, loyal behavior.

From a large point of view, the issue discussed is located between morality and crime, the state's fiscal policy and human rights. Tax fraud undermines the basic principles of "fiscal democracy", equality before taxation (Council of State, 7 February 1958, Syndicat des propiétaires de chène en liège en Algérie: 130) and in accordance with French law, an agreement as a source of consent to taxes inscribed in the Declaration of Human Rights in 1789. Fraud is a crime punishable because it undermines not only social peace (paix sociale), but also public finances.

Tax fraud is also a violation of the so-called "republican pact," which combines the relationship between individual taxpayers and society through shared values. This agreement is even more important in times of economic hardship, because the loss of the state treasury consists not only in the loss of tax liabilities, moreover, cash is not re-introduced into the economic activity. Unfair behavior should be severely punished and- in addition to recovering illegally obtained funds – potential fraudsters should be discouraged by sanctions.

In Polish practice and the theory of tax law, it is worth looking at the experience of other countries in terms of the procedure, combining the branch view in the legal system with the multidisciplinary nature of facts. Fighting fiscal fraude is a constant search for effective instruments, changing methods and approaches. Knowledge touched in the article can be useful not only for theory of law of European countries, but above all, for a European taxpayer.

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Online Cash Desks in the System of Tax Control: Features of Legal Regulation

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Abstract

Article reveals features of legal regulation of use of cash registers by settlings by cash by legal entities and individual entrepreneurs with natural persons for the rendered services, works, provided goods. The dialectic method formed a methodological basis of a research of this article. During the research such general scientific methods as scientific abstraction, system, logical, a method of the analysis and synthesis, comparative and legal were used. The conducted research develops the theory and practice of use of online cash desks in the system of tax control, allows to consider experience of foreign countries when using cash registers online for the subsequent implementation in national practice of settlement and tax legal relationship.

Keywords: Control and Cash Equipment; Online Cash Desk; Financial Law; Tax; Tax Control; Calculations; Tax Law; Budget.

JEL Classification: K34.

1 Introduction

The relevance of the considered subject is caused by development of the taxation system of any state and improvement of tax control. The purpose of this article is to analyse the content of the current tax control with use of online cash desks by subjects of the managing activity that is especially important in the conditions of development of digital economy. The main conclusion of this research is that through online cash desks taxing authorities can control the current financial transactions of subjects, their profit and the sums of assignments on taxes and fees. This way of control was

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proved in many countries, including the Russian Federation and the Republic of Poland.

During the research such scientific methods were used: analysis and synthesis, deduction and induction, systematic and comparative and legal methods. Now the large amount of works is devoted to single questions of tax control and tax administration (T. A. Guseva of «Problems of improvement of the mechanism of tax control and an order of bringing to tax responsibility» (2001), M. Orviska, J. Hunady «Selected challenges of tax administration in the context of fiscal consolidation in European countries» (2014), T.Yu. Kurbatov «Legal forms and methods of tax control» (2015), G. Schreiber «Tax practice quality control» (2012), T. Brand, A. Hodson, A. Sawyer «South East Asian tax administration issues in the drive to attract foreign direct investment: Is a regional tax authority the way forward?» (2015), A. I. Zadorozhny «Institute of tax control of transfer pricing in the Russian Federation» (2017), H. Zidkova, J. Tepperova «Registration of Sales. How to Measure Its Impact on Tax Revenues?» (2017), M. Petersone, K. Ketners «Improvement of customs and tax administration ICT system performance» (2017), C. A. Kamal Garg «Tax audit and e-filing» (2018), N. U. Richards, E. O. Ekhator «Electronic taxation in Nigeria: challenges and prospects**»** **(**2019), etc.), applications of online cash desks in an entrepreneurial activity (D. V. Panarin «Change in use of the cash register equipment in 2016: online cash desks» (2016), N. N. Buneeva «Transition to online cash desks» (2016), A. Schwanke «Tax technology: A brave new world» (2016), A. M. Saakian, A. L. Ermachenko of «Features of application of online cash desks in settlement operations of economic activity» (2018), A. Monteith «It's a digital life» (2018), J. McNally **«**Automating data flow: evolution of the compliance process» (2018) and so forth). Only in recent years works that consider online cash desks appear in the system of tax control (I. E. Kovalchuk «Online cash desks as a new form of tax control: organizational aspects and assessment of efficiency» (2017), L. A. Peseukova «Last changes in the tax legislation. online cash desks» (2017), G. V. Sitskaya, M. M. Golubeva «Online cash desks as the instrument of tax control» (2017), Radka Jerie «Czech Republic: taxation – electronic registration of sales» (2017), Yu.K. Tsaregradskaya of «Features of application of online cash desks in the system of tax control of Russia» (2018), etc.

2 Rules on use of online cash desks

Nowadays the Russian Federation reaches the new level of the development, having designated the plan of transition to digital economy till 2024. The Need of similar transition to new economic conditions was created long ago as information technologies are present at all spheres of public life and they are also given a priority from the state. However, the insufficient attention from the state to the information environment and its development led to lag of the Russian Federation in this sphere from many developed states. As a result there was initially adopted the Development strategy of information society in the Russian Federation for 2017–2030 that stated that its national interests in the field of digital economy for the state are following:

- formation of the new markets based on use of the information technologies providing leadership due to effective development of the Russian ecosystem of digital economy;
- ensuring technological independence and safety of the infrastructure connected with sale of goods and rendering services, etc. (The presidential decree of the Russian Federation, About the Development strategy of information society in the Russian Federation for 2017–2030, 2017, Article 2901).

Based on the objectives, the state adopts the "Digital Economy of the Russian Federation" program which recognizes that this economy represents economic activity for which the basis of production is the data in a digital form promoting formation of information and communicative space taking into account requirements of society, also the development of information infrastructure and formation of a technological basis for the social and economic environment (The order of the Government of the Russian Federation, About the approval of the "Digital Economy of the Russian Federation" program, 2017, Article 5138).

One of the main directions of this Program is the legal regulation of the processes connected with formation and existence of digital economy. In this regard the main goal of this regulation is the formation of such regulatory environment which would provide a favorable legal regime for development of modern information and communicative technologies and also for implementation of the economic activity connected with their use.

One of sections of the Program is devoted to implementation and use of the innovative technologies in the financial market providing the bills and legal initiatives connected with increase in a share of non-cash payments in the general system of settlement legal relations.

As the expected results the following were planned:

- a) lack of requirements to issue cash vouchers in paper form and embedding of the cash equipment in the case of automatic devices for calculations;
- b) cancellation of additional license requirements to operators of fiscal data (Government commission on use of information technologies for improvement of quality of life and conditions of maintaining an entrepreneurial activity, the Plan of measures of legal Regulation of "Digital Economy of the Russian Federation" program, 2017).

3 Tax control features in modern conditions

These innovations are necessary not only for improvement of the settlement relations between natural and legal entities, but also for improvement of tax control in the state.

Tax collection is one of the main living conditions for the modern state and for the development of society on the way to economic and social development. Process of transition to the market relations revealed the whole complex of the problems, new to economy of Russia, connected with cardinal change of nature of relationship between taxpayers and the state. Formation of new taxation system provoked the problem of mass evasion of taxpayers from tax payment. This was caused by the growth of private sector in economy which revealed a certain contradiction between the interests of the state and society on the one hand, and new owners on the other hand. This contradiction was reflected in desire to increase incomes by tax evasion. As practice shows, the question of paying or not paying taxes, or if paying in what amount, is the issue that entrepreneurs solve at the stage of calculation of payback of the commercial project. The answer to such question has to be unambiguous: to pay, as this is the only lawful way of conducting economic activity which will enable the state to exist and create conditions for an effective entrepreneurial activity. However, effective national economy

demands existence of the developed system of the state tax control including the system of legal forms and methods of checking legality, expediency and correctness of actions for formation of monetary funds at all levels of public administration.

Carrying out financial activity, the state accumulates, distributes and spends funds of money for realization of the public functions. The main object of financial activity of the state is public finances. In the course of financial activity the content of the main functions of finance – distributive, regulating and control are revealed.

Control function of finance is expressed in the fact that they represent a source of information about the condition of entire state. With a financial system, by means of controlling money, a successful (or less successful) development of the entire state and society in general is exercised. By means of finance the state keeps track of efficiency and expediency of the administrative decisions made by him and also controls correctness and the sequence of application of such decisions.

The main source of formation of public foundations of money is tax income. The value of taxes when forming budget revenues is very high. Controlling function is also a characteristic of taxes as to a specific type of finance. By means of this function the state estimates balance, and rationality of the taxation system, checks its efficiency in the existing economic conditions. Besides, by means of this tax function, compliance of actions of taxpayers to the established rules of conduct is defined.

According to P. M. Godme, the state, establishing taxes, uses enforcement measures for collecting them (Godme, P. M., 1978: 371). In this context expression of the tax control function is shown in activity of public authorities whose main objective is finally to provide taxation. This activity represents a special type of financial control – tax control.

It is necessary to emphasize that tax control and the control tax function are not identical concepts. Content of the last category is much wider as this specified tax function can show up at different stages of development of tax policy of the state. As the special type of financial control, tax control is limited to the activity of special authorities directed at fulfilling tax payment obligations by each person.

Subjects of tax control are the public authorities allocated according to the existing tax legislation of Russia powers on carrying out actions and tax control measures concerning the checked legal entities and individual entrepreneurs. Tax control is carried out by public officials of taxing authorities in various forms of tax control: tax audits, receiving explanations from individual entrepreneurs and legal entities and so forth. Court practice also emphasizes exclusivity of powers of taxing authorities in the field of tax control, specifying that courts have no right to substitute taxing authority and to carry out tax audit, but have to check legality of the decision of taxing authority (Boltinova, O. V., Tsaregradskaya, Yu.K., 2017: 26).

The main objectives and purposes of tax control:

- ensuring compliance with the current legislation by taxpayers. The legality in activity of legal entities and individual entrepreneurs is shown in respect for financial and tax discipline;
- ensuring completeness and timeliness of payment of taxes and fees. The tax legislation of Russia provides different forms of tax control allowing to define honesty or dishonesty of the taxpayer;
- assistance in correct accounting, tax accounting and reporting. Fulfillment of their obligations by taxpayers to state is possible only if all financial transactions are reflected in business and tax accounting documents in due time;
- identification and suppression of violations in the sphere of taxation. The taxing authority has to carry out checking of natural and legal entities, reveal tax violations, obtain the evidence of violations. Based on the results obtained from the studied materials, the authorities make decision on involvement of the person to tax responsibility.

Proceeding from the maintenance of the above-stated tasks, it is necessary to draw a conclusion that a main objective of tax control is ensuring the maximum receipt of all income in the budget of the state.

Tax control is of different types depending on time it is carried out: preliminary, which occurs prior to commission of financial transactions by natural and legal entities; flowing – which is carried out during these operations and the subsequent – which is possible only after financial transactions are performed.

For our research the current tax control, which happens during implementation of the settlement relations with use of online cash desks, is of interest.

4 Use of online cash desks for the current tax control

In this regard since 2017 spread the online cash desks by calculations allowing to improve tax administration in the Russian Federation (The act of the Russian Federation, About introduction of amendments to the Federal law "About Use of the Cash Register Equipment by Cash Monetary Calculations and (or) Calculations with Use of Payment Cards" and separate acts of the Russian Federation, 2016, Article 4223).

Now the practice of the settlement relations develops, therefore, that when rendering the services paid with cash:

- legal entities should use the cash register equipment;
- natural persons (including individual entrepreneurs)should use the cash register or to issue the form of the strict reporting (The act of the Russian Federation, About application of cash monetary calculations and (or) calculations with use of electronic payment instruments, 2003, Article 1957).

By the new rule legal entities and individual entrepreneurs have to use cash register equipment models with fiscal stores of data which allow to report data on the performed operations with cash or with use of cash cards through operators of fiscal data to taxing authorities online. Operators of fiscal data are the organizations that have the legal permission to data processing from tax administration of Russia.

Federal taxation service (FTS) initiated the implementation of online cash registers to the system of the settlement relations and also at first started the pilot project of their use in a number of territorial subjects of the Russian Federation in 2014–2015. (The resolution of the Government of the Russian Federation, About carrying out in 2014–2015 an experiment on use of the cash register equipment at implementation of cash monetary calculations and (or) calculations with use of payment cards for improvement of an order of its registration and application, on 16 July 2014). The made experiment showed efficiency of technology of information transfer

about the calculations made by legal entities and individual entrepreneurs and convenience of use of such technology.

The main objectives which were set by FTS at implementation of this experiment and were reached by means of introduction of online cash desks consist in the following:

- information transfer about calculations in electronic form to the address of FTS through operator of fiscal data;
- a possibility of electronic registration of the cash register equipment without visiting taxing authority and without its physical granting;
- forming of a system of identification of violations of financial discipline on the basis of the automated analysis of information on calculations and conducting tax audits.
- involvement of consumers in public control.

The legislator, making changes into use of the cash register equipment, left the right not to apply it for some categories the persons who are engaged in certain types of an entrepreneurial activity (The Tax Code of the Russian Federation. Part 2, 2000).

When using online cash desks in the course of implementation of payments by cash and (or) cash cards, the legal entity or the businessman can send the check or the form of the strict reporting in electronic form by phone or the e-mail if until calculation the client tells him data, necessary for information transfer. This innovation has both positive, and negative sides, on the one hand, the client can be sure that he will not lose the check and in case of need can show it, and on the other hand – not each client will show willingness to provide the phone number or the e-mail address because will not want to receive unnecessary advertizing messages from various subjects of economic activity.

Besides, it is necessary to consider that the cash desk can work also in offline mode when temporarily or constantly there is no Internet. It can be for various reasons: temporary failure in operation of technical means or lawful permission to use of offline mode. In the first case – data transmission will happen after elimination of technical failures as information on payments is stored in all cash registers within 30 calendar days. In the second case – there is a list of the territories remote from communication networks

where it is authorized to apply offline cash desks, the list of these territories is defined by public authorities of the territorial subject of the Russian Federation (The letter of the Ministry of Finance of the Russian Federation, 2017). At the level of the Russian Federation the criterion for definition of such territories in compliance with which was established the Ministry of Telecom and Mass Communications of the Russian Federation established that the population in such territory has to be no more than 10 000 people (The order of the Ministry of Telecom and Mass Communications of the Russian Federation, 2016).

5 Violation of the rules of using online cash desks: features of court practice

Illegal actions of legal entities and individual entrepreneurs in making cash payment has been revealed by the rules of using the cash register equipment, for the solution of this situations the Supreme Arbitration Court of the Russian Federation makes explanations about actions that can entail administrative responsibility.

The court notes that legal entities and individual entrepreneurs can perform cash monetary calculations without use of the cash register equipment in the cases provided by the legislation. Using the cash register equipment can only be avoided when issuing the strict responding forms to clients, otherwise administrative responsibility for implementation of cash monetary calculations without use of such equipment for legal entities and individual entrepreneurs is provided. It is emphasized that the legislator provides such rule only when rendering services to natural persons.

In addition, the provisions identifying particular categories of enterprises due to their production specifications or location features, and allowing them to perform monetary operations with individual entrepreneurs without online cash register, no longer apply since year 2003.

The court is especially focuses on cases of administrative prosecution for non-use of cash register equipment while selling of alcoholic products as it is necessary to apply responsibility for violation of rules of sale of separate types of goods, but not for violation of special rules of retail of alcoholic products.

Also the court pays attention that the persons which are carrying out an entrepreneurial activity without formation of legal entity are made responsible as public officials if exceptions are not provided.

6 Foreign experience of use of online cash desks in settlement legal relationship

Analyzing foreign experience, it should be noted that application of online cash desks is widely used in a number of foreign countries, such as Belgium, Bulgaria, Belarus, Poland, Serbia, China, South Korea, Ethiopia, etc., and this experience is estimated as positive as allowed to fill up the budget with additional money [Zhigulina, Yu.M. 2017: 9; Schreiber, G. 2012: 43(11)].

In the Report of OECD "Electronic abolition of sales: the threat to tax revenues" is noted that the countries fight in various ways with concealment of sales. One of ways consists in use of a certain equipment and the software. Among the countries that use this method are Greece, Italy, Poland, Turkey.

Poland much earlier, than Russia began to use online cash desks. A legal basis of use of the cash equipment in Poland is Law on tax on goods and services that states the duty of the taxpayers who are carrying out sale to the natural persons who are not conducting economic activity may keep account by means of cash registers (Law on tax on goods and services, 2004). Besides, the legislator provided two cases of release from use of cash registers: on the maximum sum of a turnover and of the nature of activity (Order of the Minister of Finance, 2014, Art. 1544).

The Ministry of Finance of Poland in 2018 planned transition from cash registers with paper checks to online cash desks, especially in the industries that are subject to risk of tax fraud. Data on these devices will come to the central computer system of the Ministry of Finance, providing daily information on fiscal reports, checks, including cancelled checks and also invoices. These measures, according to the Ministry, will allow to optimize fight with a shadow economy by means of effective control of retails and to increase tax revenues in the budget.

7 Conclusion

Use of digital technologies, by both public authorities and businessmen, allows to carry out effective interaction between them, creating the database on taxpayers who can be controlled in the online mode during performing financial transactions and payment of taxes and fees. During this process the information space of tax payers is being developed.

Technologies of management Big data allow to distinguish a number of advantages for each participant of the tax relations and for national economy in general. For taxing authorities – it is a possibility of improving quality of tax administration. For business it enables getting service in any place of the state from any device.

Nowadays this is possible to be realized by taxing authorities using digital instruments of tax control, in particular online cash desks.

Thus implementation of online cash desks in the system of financial legal relationship allows to make not only open cash settlings between legal entities and individual entrepreneurs with natural persons, but also promotes effective implementation of tax control that is confirmed by experience of various states. The main objective of a research consisting in the analysis of legal regulation of use of online cash desks in the system of tax control was reached as legal acts regulating this sphere in the Russian Federation (The Tax Code of the Russian Federation, the federal law "About Use of the Cash Register Equipment at Implementation of Cash Monetary Calculations and (or) Calculations with Use of Payment Cards", etc.) and the Republic Poland were analysed (Law on tax on goods and services, 2004). The analysis of these acts showed that they fix rules of daily transfer to taxing authorities of information on operations and the received sums of money and also transition from paper checks to electronic. In this regard the real research confirms the author's hypothesis that through online cash desks taxing authorities carry out check of the financial transactions of businessmen in the online mode. This way of tax control proved positively in many countries, in particular in the budget of Georgia for 2012 tax revenues increased by 65 % thanks to online cash desks in an entrepreneurial activity.

This experience shows that any country is interested in using online cash desks. This gives an opportunity to monitor incomes of legal entities and natural persons in real time and also enables control of potential tax revenues.

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VAT – SELECTED ISSUES

Evolution Trends of Polish Substantive Tax Law Aimed at Limiting Fraud in the Value-Added Tax

Witold Modzelewski[1] et al.[2]

Abstract

The subject of this paper is the latest evolution of substantive tax law aimed at limiting fraud in the value added tax. This tax in its harmonised version, in force in Poland since 2004, has become a field of mass abuses, resulting in a unique scale of tax evasion and extortion of tax refunds. Due to a real and temporary nominal decrease in income from this tax (in the years 2007–2016), attempts were made to counteract this phenomenon. The article provides a theoretical classification of these activities, distinguishing in particular: changes in substantive law to close loopholes allowing for tax evasion or obtaining undue refunds, the introduction of new information or denunciation obligations to facilitate the detection of these abuses, and the extension or increase of repressive sanctions for abuse of this tax. Then, the four main important groups of changes introduced during this period are discussed, namely: (i) Standard Audit File for Tax [SAF-T] (information submitted periodically or at the request of the authorities); (ii) a split payment (voluntary and planned mandatory); (iii) Clearing House's ICT System [STIR], new sanctions for forgery or use of forged invoices. The solutions put in place in 2016–2018 have had a deterrent effect, but their limited practical application and too short duration do not allow for a precise estimation of their effectiveness in curbing tax fraud. However, these solutions provide the first valuable experience in the fight against these abuses and should be improved.

Keywords: Financial Law; Tax Law; Budget Law; Legal Process; Public Finance.

JEL Classifications: K34; P45.

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1 Introduction – The evolution of Polish tax law under the Third Republic (since 1989)

Spanning almost thirty years now, can be conventionally divided into the following five stages: First, the years 1989–1991 saw a hastened and, probably, deliberate destruction of the law that had been shaped under the previous political system, alongside using public levies for non-fiscal purposes (discrimination of the public and cooperative sectors) and, simultaneously, a degradation of the tax law's fiscal function, all of which eventually led to a breakdown in the budget revenue that was unprecedented in the post-war period. Second, in 1992–1997 came the first, and hitherto the only, period of rebuilding the tax law and reinstating its sufficient fiscal efficiency: most of the conceptual solutions were developed for the tax system and put into practice at the time (some of them remaining in force today), along with the largest, nominal as well as real, increase in the budget revenue recorded over the last thirty years. Third, the years 1998–2003 witnessed the first, though partial and inconsistent, deviation from the improvement trend in the fiscal efficiency of the tax law; this was correlated with a real, or even nominal (though slight) decrease in the budget revenue. It was then that first symptoms of internal destruction of the tax law, affected as it was by tax/fiscal stakeholders and business ('privatisation of the tax law'). Fourth, the years 2004–2016 were marked by the 'Community period' in Polish tax law which, along with the real and apparent implementation of European-Community solutions, underwent a fast destruction. This occurred in parallel with a drop in the fiscal (tax) efficiency, the second such within twenty-five(-or-so) years, against a fast-increasing tax loophole, and a real *and* nominal drop in the budget revenue (not as deep as that observed in 1989–1991, though). Last, in the period 2017–2018, attempts were made at improving the fiscal efficiency of the tax law and (partly) eliminating the effects of the law's destruction in the preceding two periods.

This article seeks to describe the most recent revolution in Polish tax law, which was designed to eliminate or restrict abuse (in a variety of aspects) in the value-added tax (VAT), the most important tax in, roughly, the last twenty-five years. We focus on legislative actions aimed at increasing the fiscal

efficiency of VAT. The amendments made to (or, changes in) the tax law in this respect need to be classed into five groups, in theoretical terms:

- changes/amendments to the substantive tax law whose object is the rights and obligations of taxpayers (taxable persons) and payers relating directly to the determination of the object of taxation and the tax base, the output tax, and the tax obligation. This change is meant to eliminate gaps in the regulations and to amend or modify the wording/phrasing of those regulations which were drafted resulting from errors or legislative lobbying, thereby causing deteriorated fiscal efficiency of the law in question ('closing the legal loopholes');
- information-related changes consisting in imposition on entities operating under the tax law the obligation to provide the competent authorities/bodies with their tax settlements data ('broader self-denouncement');
- changes regarding the competencies of the relevant authorities/bodies and in the law regulating the rules and procedure of control inspection of tax-law legal entities, aiming at detecting cases of escape from taxation ('expanded public oversight');
- denunciation made obligatory to third parties, the focus being activities of tax-law legal entities which may result in escape from taxation ('third-party denunciation obligations');
- extended scope, or increased repressiveness, of the law, relative to escape from taxation and tax-refund fraud ('increased repressiveness').

The fiscal efficiency of individual taxes where tax liabilities occur by operation of law (the principle) is principally conditional upon the three indispensable factors:

- quality of the legal construct of the tax in question and, primarily, the content of substantive law provisions that regulate the construct's elements, the indispensable elements in particular (i.e. the subject/entity, object of taxation, tax base, rates of tax, and payment conditions), in a way as to formally prevent or considerably hindering escape from taxation;
- legal construct of documenting/evidencing, recording, and declaring tasks that enforce the disclosure of the real amounts of elements of the tax's construct;

- proportional repressiveness of the system of sanctions for breach of the right to potential benefits achieved by tax-law legal entities infringing the rules set out in (a) or (b) above.

In the event that the provisions regulating the factors specified in (a) and (b) prove defective or insufficient/inefficient, the significance of the other methods of improvement of fiscal efficiency is downright illusory, especially when the factors specified in (2)–(4) are concerned.

The following sections describe the most important changes/amendments made to Polish substantive tax law in 2015 to 2018 with the declared objective to limit abuse related to VAT.

Obligatory submission of information regarding tax records kept for VAT purposes.[3]

Under the Act of 10 September 2015 'on the amendments to the General Tax Regulations Act and to certain other acts or laws'[4], certain VAT taxpayers (so-called 'big entrepreneurs') have been obligated, effective 1 July 2016, to submit the so-called Standard Audit File for Tax (SAF-T (Polish, JPK_VAT)] comprising data from the VAT registers to the Ministry of Finance, on a monthly basis. As from 1 January 2017, the said obligation has been extended to medium- and small-sized entrepreneurs; from the beginning of 2018 onwards, the task has been made obligatory also for micro-enterprises. SAF-T is structured so as to provide information on purchases/acquisitions and sales, based on the taxpayer's VAT records for the respective period. The form is sent in an electronic format only, by the 25th day of the month, as for the preceding month, even though the taxpayer settles his accounts on a quarterly basis.

3 M. Jendraszczyk, 'Projektowane zmiany w zakresie likwidacji obowiązku składania przez podatników podatku od towarów i usług niektórych deklaracji i informacji', Biuletyn Instytutu Studiów Podatkowych 2/2019 (270), p. 10; M. Szymocha, 'Jednolity Plik Kontrolny – wybrane zagadnienia', Biuletyn Instytutu Studiów Podatkowych [hereinafter, BISP] 7/2016 (239), p. 20; M. Szymocha, 'Jednolity Plik Kontrolny – struktury JPK_KR, JPK_WB, JPK_VAT', BISP 8/2016 (240) p. 22.
J. Włoch, P. Gaszek, 'JPK_WB – nowy projekt Ministerstwa Finansów jako narzędzie w walce z oszustwami i nadużyciami występującymi w podatku od towarów i usług', (New project of Mnistiry of Finance – new instrument in the fight of criminal fraud and misusuage in area of VAT) BISP 7/2017 (251), p. 5.

4 Journal of Laws [JL] 2015, Item 1649, as amended.

Under Art. 109, clause 3 of the Act of 11 March 2004 on the Value Added Tax[5], taxpayers [resp. taxable persons], save for taxpayers only performing actions exempt from tax are obligated to keep tax records comprising data indispensable for appropriate drafting of tax return and of the recapitulative statement. The records ought to specify, in particular, the data indispensable for determining the object of taxation and tax base, the actual amount of the output tax, adjustments of output tax, the amount of input tax reducing the output tax amount, input tax adjustments, the amount of tax payable to the Tax Office or reimbursable therefrom, as well as any other data that may contribute to identification of individual transactions – including the number by which the contracting party is identified for purposes of VAT or another relevant tax. As per Art. 82, § 1(b) of the General Tax Regulations Act of 29 August 1997[6], legal persons/entities, organisational units without legal personality, and natural persons keeping tax books with use of IT programmes are obligated to provide the Head of the National Tax Administration, without being summoned or requested to do so by the tax authority, with use of electronic means of communication, with details of the records they keep as referred to in Art. 109, clause 3 of the VAT Act of 11 March 2004, in an electronic format that corresponds with the logical structure referred to in Art. 193a, § 2, observing the rules regarding the sending of tax books/registers of parts thereof, as laid down in the regulations issued under Art. 193(a), § 3, for then monthly periods, by the 25th day of the month following each consecutive month, and pointing to the month concerned.[7]

2 Information submitted on demand of tax authorities[8]

As from 1 July 2018, pursuant to the Act of 10 September 2015 amending the General Tax Regulations, all the taxpayers who keep tax registers

5 JL 2018, Item 2174, as amended.

6 JL. 2018, Item 800, as amended; hereinafter referred to as the 'General Tax Regulations'.

7 In line with Art. 193a, § 2 of the General Tax Regulations, the logical structure of the electronic format of tax(ation) records (books) and accounting documents/vouchers, including the option for them to be generated using IT programmes commonly used by entrepreneurs and automated data analysis, is available at the Bulletin of Public Information [BIP], 'entity website of the office handling the Minister in charge of public finance'.

8 K. Wawrzonkiewicz, 'JPK na żądanie organów podatkowych', BISP 7/2018 (263), p. 44.

or books and generate accounting documents/vouchers in electronic format, are tasked with submitting SAF-T structures on demand of tax authorities in the course of audit/checking activities, tax inspection, customs and fiscal inspection, and tax proceedings. As explained by the Ministry of Finance, "*… in the event that the taxpayer keeps his tax books in hardcopy format, he shall not have to generate a SAF-T upon demand of the tax authorities; the tax authorities would, accordingly, only demand hardcopy documents during an inspection. Upon demand, SAF-T structures will only be provided by those taxpayers who already keep their tax books in electronic format*."[9]

In line with Art. 193(a) § 1 of the General Tax Regulations of 29 August 1997, for tax records kept with use of IT programmes, the competent tax authority may demand that such records (books) and/or accounting documents (vouchers) be supplied with use of electronic means of communication or on IT data carriers, in appropriate electronic form.[10]

Upon request of the authority, within no shorter than three (3) days (the exact time-limit to be stated in the request), files have to be rendered available for the following structures: books of account [JPK_KR]; bank statements [JPK_WB]; warehouse (external deliveries received, inventory issues, goods issues, inter-warehouse transfers) [JPK_MAG]; invoices (broken down) [JPK_FA]; revenue and expense ledger [JPK_PKPIR]; revenue/income registry [JPK_EWP]. As per § 3, clause 1 of the Ordinance of the Minister of Finance of 24 June 2016[11], IT carriers of data whereon the books may be recorded and delivered, are to be marked in a way enabling unambiguous identification of the carrier.

On demand of the authority, SAF-T [JPK] structures are used for purposes of audit/checking activities, tax proceedings, or tax inspection and customs and fiscal inspection. As part of these procedures, taxpayers submit tax books/registers and accounting documents/vouchers being subject to no adjustments whatsoever.

9 Https://www.finanse.mf.gov.pl/web/wp/pp/jpk/pytania-i-odpowiedzi
10 See ftn. 5.
11 Dz.U. z 2016 r. poz. 932.

3 Split payment mechanism[12]

As from 1 July 2018, a new section was added in the VAT Act of 11 March 2004, entitled 'The Split Payment Mechanism' (Art. 108(a)–(e)). The rationale behind the solution is, essentially, that payment for the commodity or service purchased is made so that the payment amount correspondent with the net selling amount may be paid by the purchaser to the supplier's settlement account, or be settled otherwise, whereas the remaining payment, corresponding with the VAT amount, may be paid to the supplier's VAT-related bank account. Art. 108(a) added to the VAT Act regulates the essentials of the split payment mechanism: taxpayers who have received an invoice, within the meaning of Art. 2, item 21 of the said Act, specifying the amount of tax, may apply the split payment mechanism upon making the payment for the goods or services purchased. Thus, the initiative to apply the mechanism under discussion is left to the discretion of the purchaser of the goods/service(s), whilst the actual application depends upon consent from the parties to the agreement based whereupon the payment is made. The payment for the purchased commodity or service is made with use of the transfer message in the way that payment of the amount, in whole of in part, that corresponds with the net value of the sale is paid by the purchaser to the settlement account at the bank or to the account at the savings and credit union, whereas the remainder of the payment, correspondent with the entire VAT amount or a part thereof, is paid to the VAT

12 Council Implementing Decision (EU) 2019/310 of 18 February 2019 authorising Poland to introduce a special measure derogating from Article 226 of Directive 2006/112/EC on the common system of value-added tax, OJ L 51/19 of 22 February 2019; K. Lewecki, 'Podzielona płatność – metody wyłączające niekontrolowane wpływy na rachunek VAT', BISP 8/2018 (264), p. 17; W. Modzelewski, 'Podzielona płatność w podatku od towarów i usług: koncepcja, doświadczenia, wnioski', BISP 01/2019 (269), p. 10; M. Unisk, 'Podzielona płatność w VAT od lipca 2018 r. (cz. 1). Podstawowe założenia i cechy systemu', Podatkowych BISP 05/2018 (261), p. 42; M. Unisk, 'Podzielona płatność w VAT od lipca 2018 r. (cz. 2). Podstawowe założenia i cechy systemu', BISP 06/2018 (262), p. 60; M. Unisk, 'Podzielona płatność w VAT od lipca 2018 r. (cz. 3). Podstawowe założenia i cechy systemu', BISP 06/2018 (263), p. 35.

account being a special account wherein cash is collected related to payment of VAT incumbent on the taxpayer.[13]

The basic methods of administering by the taxpayer of the cash collected in his VAT account include payment to the counterparties of the amount of tax disclosed on the purchase invoices received from them, and payment of the VAT tax liability to the Tax Office. Article 108(c) of the VAT Act has introduced a limited system of incentives for those taxpayers who have resolved to voluntarily employ the split payment mechanism. In specific, when an invoice is paid with use of the mechanism, the joint-and-several responsibility provisions do not apply; similarly, not applicable are the regulations related to the launch of sanctions defined in Art. 112(b), clause 1, item 1, and clause 2, item 1; and, in Art. 112(c) of the VAT Act, up to the tax amount corresponding with the amount specified in the invoice received and paid with use of the split payment mechanism.

On 18 February 2019, the Council of the European Union issued an implementing decision (2019/310) that authorised Poland to introduce a special measure – namely, an obligatory split payment mechanism – being a derogation from Article 226 of Directive 2006/112/EC on the common system of value-added tax. Poland applied for authorisation to introduce the special measure, as a derogation from the said article, in order to apply the split payment mechanism to invoices issued in relation to supplies of goods and provision of services prone to fraud and, basically, ones to which the reverse charge mechanism and joint-and-several responsibility are pertinent in Poland. Poland applied for such special measure for a period of three years, from 1 January 2019 to 31 December 2021, arguing that employment

13 The technical parameters of the transfer message are not regulated in a separate act of law. The Act clearly points to the scope of information to be obligatorily specified in the transfer message. The taxpayer is to fill out the transfer message which specifies two amounts: the gross amount of sale and the tax. The Bank or the Cooperative Savings and Credit Union [SKOK], on its part, takes action aiming at transferring the paid amount to the appropriate accounts – namely, the amount correspondent with the tax goes to the VAT account whereas the remainder is credited to the settlement account at the Bank or the Union. For payments made to a taxpayer other than specified in the invoice, the taxpayer to whom the payment was made is responsible, on a joint-and-several basis, together with the supplier of the goods or services for the tax unsettled by such a goods/services supplier and related to the supply (delivery) concerned, up to the amount received on the VAT account.

of a special measure in the form of compulsory split payment mechanism would help to eliminate frauds related to VAT. What the split payment mechanism essentially does is that the VAT amount deposited on a separate VAT account of the supplier/service provider (taxpayer) may only be used for a limited purpose – namely, for payment of a VAT tax liability to the tax authority, or for payment of the VAT as disclosed in the invoices received from suppliers/service providers. Hence, the mechanism in question ensures, to a higher degree, that the tax authorities will receive the due (output) tax in its entire amount.

The positive decision of the EU Council has paved the way open for the Polish legislator to take legislative action in areas highly vulnerable to VAT-related fraud. The economy sectors concerned include steel, scrap metal, electronic equipment, gold, non-ferrous metals, fuels, and plastics. The reverse charge mechanism as well as joint-and-several responsibility of the supplier/service provider and purchaser have hitherto applied to such commodities, which has however not eliminated abuses in these sectors. The EU Council's decision also implies that Poland has assured the European Commission that for transactions to which compulsory split payment applies, the reimbursement will have been made within twenty-five (25) days, upon application of the taxpayer who has his VAT account blocked. The obligatory split payment mechanism is meant to apply to all the suppliers and service providers, including any suppliers (deliverers) having no registered office in Poland and hence holding a bank account kept in accordance with the Polish banking law.[14] As the Government has reassured, such entities will bear no extra cost related to obligatory opening of a bank account in Poland, whatsoever.[15]

14 The Decision renders Poland obligated to submit to the European Commission, within eighteen (18) months of the date the split payment mechanism enters into force, a report on its general impact on the level of VAT-related fraud and on the taxpayers (taxable persons) concerned by the measure. The Decision is applicable from 1 March 2019 to 28 February 2022.

15 No draft implementing regulations for the Decision in question have been compiled in March 2019.

4 Act amending certain laws or acts in order to counteract the use of the financial sector for tax fraud purposes[16]

On 24 November 2017, the Sejm (i.e. lower house of the Polish Parliament) adopted the Act 'amending certain laws or acts in order to counteract the use of the financial sector to tax fraud purposes'[17]. The amendment was primarily meant to counteract fiscal fraud and, in particular, reducing the gap in VAT caused by instances of such fraud. The Act has launched a system to potentially eliminate fictitious entities from business transactions, thereby reinforcing the economic and legal security of taxpayers in the business-trading environment. Pursuant to the Act, the Head of the National Tax Administration (NTA) analyses the risk of use by qualified entities of banks and cooperative savings and credit unions [SKOKs] for committing tax offences, particularly, VAT frauds committed by organised criminal groups (Article 258 of Polish Criminal Code) and related crimes or offences (such as issuing empty invoices). In his analysis, the Head of NTA makes use of the data he possesses, the risk rate determined by the Clearing House's ICT System [STIR], information on the account of qualified entities, within the Act's meaning, and breakdowns of transactions between qualified entities. In order to determine the risk score of use by qualified entities of banks and SKOKs for commitment of tax offences, the Clearing

16 M. Betiuk, 'Obowiązki instytucji obowiązanych w nowej ustawie o przeciwdziałaniu praniu pieniędzy i finansowaniu terroryzmu', BISP 8/2018 (264), pp. 20–23; A. Garbarczyk, 'Projekt ustawy o zmianie ustawy – Ordynacja podatkowa oraz niektórych innych ustaw w zakresie przeciwdziałania wykorzystywaniu sektora finansowego do wyłudzeń skarbowych. BISP 6/2018 (262), pp. 32–35; M. Jendraszczyk, 'Zmiany w Ordynacji podatkowej wynikające z projektu z dnia 20 marca 2017 r. Ustawy o z mianie niektórych ustaw w celu przeciwdziałania wykorzystywaniu sektora finansowego dla wyłudzeń skarbowych', BISP 5/2017 (249), p. 34.

17 The amending Act under discussion pertains to the following pieces of legislation: General Tax Regulations Act on 29 August 1997; Code of Civil Procedure Act of 17 November 1964; Enforcement Procedure in Administration Act of 17 June 1966; Act of 13 October 1995 'on the rules for recording and identification of taxpayers and payers'; the Banking Law Act of 29 August 1997; the Commodity Exchange Act of 26 October 2000; Bankruptcy Law Act of 28 February 2003; the Value Added Tax Act of 11 March 2004; the Act of 27 May 2004 'on investment funds and the management of alternative investment funds'; Trading in Financial Instruments Act of 29 July 2005; Cooperative Savings and Credit Unions Act of 5 November 2009; and, National Tax Administration Act of 16 November 2016.

House uses its IT system to process the above information and breakdowns, including items of banking secrecy and SKOKs' professional secrecy. Details of qualified entities are transferred to the STIR by financial sector entities (i.e. banks, SKOKs). To determine the rate (score), the Clearing House may also use data gathered at the Central National Taxpayer Register [CRP KEP], including data from the National Court Register [KRS], details of natural persons entered in the Central Registration and Information on Business [CEIDG], and public access data from breakdowns/lists of entities referred to in Article 96(b) of the VAT Act.[18]

Resulting from the processing of data by the Clearing House's ICT system, information on the risk rate is automatically generated, which may become the basis for NTA Head, or by a body/authority reporting to him, to take action – especially if the score indicates that the qualified entity might use the operations of a bank or a savings and credit union for a purpose related to tax fraud; one such action may consist in request to block the qualified entity's account.[19]

The risk score is the rate of use of the operations of (a) bank(s) or (a) SKOK(s) for (a) purpose(s) related to fiscal/tax fraud. The score is determined by the Clearing House in regard of the qualified entity automatically in the STIR, with use of the algorithms developed by the House which take into account the practices of the banking sectors and the SKOKs as far as counteracting the use of their operations for committing fiscal offences and crimes. In addition, the following criteria are employed:

- economic criteria – consisting in evaluation of the transaction entered into by the qualified entity with use of an account within a business environment, particularly in regard of the purpose of such entity's economic operations, or, of transactions that cannot be justified in terms of the entity's operations;
- geographic criteria – concerning transactions entered into with entities from countries with considerable threat of tax fraud;

18 Details regarding entities that have been refused registration by the Head of the Tax Office, VAT taxpayers deleted from the registry ex officio and restored as VAT taxpayers.

19 In order to verify the information he possesses, esp. risk analysis results, NTA Head is empowered to request banks or SKOKs for more data or details of relevance.

- object-related criteria – concerning business operations pursued by the qualified entity which prove highly risky in terms of proneness to tax fraud;
- behavioural criteria – concerning untypical behaviour or conduct of the qualified entity, given the situation;
- relationship criteria – investigating the qualified entity's relations(hips) with entities in respect of which there is a risk that they might participate in, or organise, actions related to tax fraud.

Transmittal of data, information and requests referred to in Section IIIB of the General Tax Regulations from the Bank's/SKOK's ICT system to the STIR; subsequently, from the STIR to the Central Register of Tax Data and, therefrom, to the Bank's/SKOK's ICT system is carried out automatically and forthwith via the STIR.[20]

In the event that there appears a legitimate suspicion of committed tax fraud, the Head of NTA, as part of his statutory tasks, notifies the competent authority empowered to pursue preliminary proceedings. A mechanism to block the qualified entity's account on request of NTA Head is also laid down by the Act. The use of this particular measure is, however, limited to cases where no softer means, which would not intervene so deeply in one's proprietorship, is considered efficient for securing the State Treasury's interest. Blockade of the account gives a much broader potential than withdrawal of a transaction, the latter always being targeted on a single specific order or instruction related to the account in question. By means of blockade, the funds transacted can be secured, along with the entire balance. Withholding a suspected transaction causes that all the parties entangled the shady dealings of fraud might carry out (an) other transaction(s) to hide the cash that has not been involved but is kept on the same account and might (have been) used to simulate the payment

20 This method of transferral of data is determined by the considerable quantity of such data. Transmission of data, information and/or requests, referred to in Section IIIB of the General Tax Regulations, between associated (affiliated) cooperative banks/SKOKs and the STIR can be done with use of ICT systems of, respectively, the associating (affiliating) bank, as understood to mean by Art. 2, item 2 of the Act of 7 December 2000 'on the functioning of cooperative banks, their association and associating banks' (i.e. JL 2016, Item 1826), or, the National Cooperative Savings and Credit Union referred to in the Cooperative Savings and Credit Unions Act of 5 November 2009.

for commodity. With the blocked account, such a situation is prevented. Hence, only the institution of blockade of qualified entity's account has been introduced, the withholding of transaction being quitted.

The blockade is effective in respect of all the entities entitled to the account in question. NTA Head may resolve to block the qualified entity's account for no longer than seventy-two (72) hours. Such a decision may be issued if the information the NTA Head has, in its entirety – in particular, risk analysis results as well as any other circumstances NTA authorities are aware of due to tax information and operational/analytical work – Is indicative of the qualified entity's possible use of the operations of banks or savings and credit unions for purposes having to do with fiscal fraud, or for operations aiming at fiscal fraud. In such circumstances, blocking the qualified entity's account is a must, in view of counteracting such effects. Assessment of these premises rests with the Head of NTA.

The funds amassed on the qualified entity's blocked account ought to be allocated to payment of the tax or customs arrears, including default interest, wherever practicable. This is what happens when the qualified entity submits a return, a correction of tax return/customs declaration, or the final decision is issued determining or confirming the tax or customs arrears – or, a non-final decision of this sort is rendered immediately enforceable. The Head of NTA resolves, by means of an ex-officio decision, whether the cash from the blocked account be set off against the tax arrears, default interest included.[21]

21 The decision is targeted at the qualified entity. Against the decision to set off the cash from the blocked account against tax or customs arrears, default interest included, application may be submitted to the Head of NTA for reconsideration of the case, or appeal to the competent Administrative Court. Such application is considered without undue delay, not later however than within seven (7) days. The request to have the final decision executed is addressed to the Bank/SKOK. Complaints against such decision are acceptable under the 'Law on Proceedings before Administrative Courts' Act of 30 August 2002, whereas the files and replies to the complaint against the decision to extend the blockade are submitted within five (5) days of the date such complaint is received (instead of the standard thirty-day period). The Administrative Court is supposed to have the complaint considered within thirty (30) calendar days of the day it receives the file together with the reply to the complaint.

5 New types of material and intellectual falsity directly associated with VAT abuses[22]

As from 1 March 2017, particular forms of the offences of material and intellectual falsity were defined (Arts. 270(a) and 271(a)) directly associated with VAT. A peculiar characteristic of these solutions is the 'invoice' – the object of causative acts. A definition of 'invoice' referring to the definition in Art. 2, item 31 of the VAT Act has been introduced in the Polish Criminal Code[23]. As per the said provision, 'invoice' shall be understood to mean a document, in paper or electronic form, containing the data required by the Act and the related secondary legislation.

Para. 1, Art. 270(a) establishes the basic type of offence consisting in forging an invoice: "*Who, in order to use it as a legitimate document, has counterfeited or processed an invoice with respect to the factual circumstances that may be of relevance to determination of the amount of a public liability or reimbursement thereof, or, of reimbursement of another tax liability, or has ever used such (an) invoice(s), shall be subject to imprisonment of six (6) months to eight (8) years*." Para. 2 regulates the qualified type whereby: "If the perpetrator has committed the act defined in Paragraph 1 in respect of (an) invoice(s) specifying a total liability whose amount, or aggregate amount, is substantial, or has made the committed offence a permanent source of income for himself, shall be subject to imprisonment of a minimum of three (3) years. Para. 3 defines a privileged type, related to minor instances. In such situations, the perpetrator

22 A. Lipnicki, 'Przepadek przedsiębiorstwa na podstawie Kodeksu Karnego jako metoda zapobiegania przestępczości podatkowej (cz. 1)', BISP 4/2017 (248), p. 46; idem, 'Rozszerzona konfiskata oraz przepadek przedsiębiorstwa na podstawie Kodeksu Karnego jako metoda zapobiegania przestępczości podatkowej (cz. 2)', BISP 5/2017 (249) p. 31; idem, 'Rozszerzona konfiskata oraz przepadek przedsiębiorstwa na podstawie Kodeksu Karnego jako metoda zapobiegania przestępczości podatkowej (cz. 3)', BISP 6/2017 (250), p. 21; idem, 'Rozszerzona konfiskata oraz przepadek przedsiębiorstwa na podstawie Kodeksu Karnego jako metoda zapobiegania przestępczości podatkowej (cz. 4)', BISP 7/2017 (251), p. 21; W. Modzelewski, 'Anulowanie faktur w świetle nowych przestępstw fakturowych, czyli o katastrofie interpretacyjnej', BISP 3/2017 (247), p. 32.
M. Sobiech, A. Sobiech, 'Przestępstwa fakturowe w świetle nowelizacji Kodeksu Karnego Skarbowego', BISP 1/2017 (245), p. 30.

23 JL 2016, Item 710, as amended; hereinafter referred to as the 'VAT Act'.

shall be subject to a penalty of fine, restriction of liberty, or imprisonment of up to two (2) years.

Also, the scope of facts whereto criminalisation of the provision in question pertains has been expanded; namely, the respective item has been rephrased as: "…factual circumstances that may be of relevance to determination of the amount of a public liability or reimbursement thereof, or, of reimbursement of another tax liability…". This amendment confirms the view whereby situations describable as unsubstantiated reimbursements (instances of fraud), being, essentially, the ratio legis behind the amendment under discussion, has been made part of the provision in question.[24] However, the phrase 'another tax liability' is not completely clear: as a matter of fact, the description 'public liability' completely covers the term 'tax-law liabilities'.[25]

It has to be noted that on the subject side of the offence the issuer of such invoice appears along with the entity that uses such document. In consequence of the thus-set objective scope, this norm may potentially prove to be ideally concurrent with the provisions of the Polish Fiscal Penal Code [hereinafter, 'PFPC'] (cf. Arts. 56, 62, and 72 of the Fiscal Penal Code Act of 10 September 1999[26]) and cumulatively concurrent with the Polish Criminal Code (particularly, Art. 286 of PCC).

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24 It has to be pointed out that counterfeiting of invoices that might be of relevance to determination of the amount reimbursable will, as a matter of fact, be preceded by a change in the circumstances of relevance to determination of the public liability. In spite of this ascertainment, one might have concluded in the course of interpretation that the intention limited to obtaining the reimbursement would have precluded the penalisation of the earlier phase (thus, inadvertence would have extended to a 'forefield act'). Yet, the amendment in question has removed any interpretive doubts in this respect.

25 In line with the amendment under discussion, the phrase "… value/amount, or aggregate value/amount, is substantial…" should be comprehended in terms of a value (amount) in excess of one million zloty (PLN 1 000 000) at the moment the offence is committed. The legislator has namely defined this description in reference to the legal definition of 'assets of substantial value' (*resp.*, 'substantially valuable assets' in Para. 6, Art. 115 PCC. The phrase 'permanent source of income' likewise calls for explanation. The criminal law doctrine has it that a Law never requires anything beyond permanence of the source of income coming from the committed offence, it being irrelevant whether the perpetrator has any other, parallel source of income.

26 I.e. JL 2013, Item 186; hereinafter, 'PFPC'.

The amended version of Art. 271(a) PCC typifies a peculiar type of falsity that may assume the form of intellectual as well as material falsity. Such ascertainment is based on the interpretative process of the provision in question; in contrast to the classical intellectual falsity as regulated in Art. 271 PCC, where individual offence proper is stipulated (as one that may only be committed by a public functionary or another person entitled to issue the document), the subject party in Art. 271(a) has been rendered more precise by the use of the subjective pronoun 'who'. Consequently, the offence's subjective scope will include entities entitled to issue the invoice alongside 'regular forfeiters' whose status is not necessarily that of VAT taxpayers.[27] The offence in question appears in two types. The basic type appears where the invoices specify an aggregate amount of total liabilities whose value or aggregate value is considerable: then, the perpetrator is subject to imprisonment of six (6) months to eight (8) years. In parallel, a qualified type has been introduced, being the case when the perpetrator has issued (an) invoice(s) amounting to such total liabilities whose amount, or aggregate amount, is substantial, or, has made the committed offence a permanent source of income for himself. In the later case, he shall be subject to imprisonment of a minimum of three (3) years. 'Substantial' amount or value refers to an amount/value which is in excess of two-hundred thousand Polish zloty (PLN 200 000) at the moment the criminal act (offence) is committed.

In discussing the objective aspects of the offence in question, it has to be emphasised that it extends to the invoice's issuer as well as the one who has made use of such invoice (cf. Art. 271(a), Para. 1, *in fine*: "… *or has ever used such (an) invoice(s)*…".[28]

27 The actual action of issuance of an invoice may be done by the authorised as well as unauthorised entity.

28 As part of the amendment, it has been resolved that, on an additional and extraordinary basis, more severe penalties for the aforementioned offences will be provided for. As per Art. 277(a): "Who has committed an offence determined in Article 270(a), Para. 1, or in Article 271(a), Para. 1, with respect to (an) invoice(s) that specify the total amount of liabilities whose value, or aggregate value, is in excess of five-fold the amount determining a property of substantial value, he shall be subject to penalty of imprisonment of no less than five (5) years, or penalty of twenty-five (25)-year imprisonment." What this regulation means is that for perpetrators who have issued fictitious (or, unreliable) invoices at an amount exceeding five million zloty (PLN 5 000 000) or have made use of any such invoice, envisioned will be the option to apply much more severe type of penalty – up to twenty-five years of imprisonment.

6 Amendments to Polish Criminal Code versus related provisions of Polish Penal Fiscal Code

The amendment discussed in item 7 introduces to the Criminal Code much higher penalties related to falsification and counterfeiting of invoices and to using of the same. The tightened penal respobsibility related to such offences is primarily related to the previously inefficient struggle against tax crimes. In consequence of the amendment, the Criminal Code has taken over a considerable amount of crimes/offences related to fraud and unlawful reductions of tax amounts payable. Let us note that such types of offence tend to coincide, as it were, with those addressed by the Fiscal Penal Code – particularly, those typified in Arts. 56, 76, and 62 PFPC. It should be emphasised that in case of concurrence of offences under both the PCC and the PFPC, the directive expressed in Article 8, Paras. 1 and 2 of PFPC shall apply; thereby, "If the same act which is a fiscal offence or tax misdemeanour bears also the attributes of an offence or crime specified in the criminal legislation of other law, each of these provisions shall be applied. Only the most severe penalty is subject to execution, which does not prevent the execution of penal measures or other measures adopted on the basis of all concurrent provisions. The criminal measures and safeguards and supervision is used, even if it was adjudicated only on the basis of one of the concurrent regulations; in case of adjudication for concurrent offences of prohibitions of the same kind or deprivation of civil rights, the court shall apply the provisions of the total penalty."

Attention should be paid, in particular, to a threat ensuing to honest taxpayers who, having encountered a dishonest counterparty, have come into possession of a counterfeit invoice. The point is about classical offences based on the 'missing trader' construct: in such cases, taxpayers completely unaware of what might occur get involved in criminal mechanisms, as their designed role is to additionally authenticate the overwhelming criminal structure. Under the amendment under discussion, such persons will doubtlessly fall under the hypothesis of Arts. 270(a) and 271(a). therefore, in connection with the above-described consequences ensuing from ideal concurrence of offences, their acts will be classified as criminal offences. It should

be remarked at this point that the perpetrator's entry into the area of penal criminalisation will prevent application of the benefactions of exclusion or limitation of penalisation, as otherwise provided by the PFPC. Consequently, the entity that has used a counterfeit invoice will not be able to use institutions such as voluntary disclosure under Art. 16 PFPC or, primarily, exclusion of penalisation through legally efficient adjustment of tax return (Art. 81, Para. 2 of the General Tax Provisions Act of 29 August 1997[29], in conjunction with Art. 16(a) PFPC). What is more, given the circumstances, submittal of adjusted tax return would be, as it were, an act of self-denunciation that would criminate the perpetrator while giving him no additional rights whatsoever. Let us emphasise, in parallel, that an entity that has used incorrect invoices amounting to PLN 200 000 may be subject to severe penal liability.

7 Amendments to penal fiscal law

The changes introduced by means of yet another amendment to the Fiscal Penal Code are made to implement the postulate to tighten up the responsibility for causative acts resulting in enormous frauds in VAT.[30] The modification is primarily meant to tighten up the liability for persons issuing 'empty invoices'. It should be noted in this context that penal sanctions are oftentimes the only real threat posed to such entities; the point is, the perpetrators of such torts are, usually, 'fronts' or 'personal endorses' who have no actual property or assets by themselves. Hence, the administrative responsibility under so-called tax sanction provided in Art. 108 of the VAT Act brings about no measurable results with regards to them (the recoverability of related dues is merely around 1–2 %). As per the amendment, Para. 3, Art. 9 of the Fiscal Penal Code Act of 17 October 1999 is to be amended so that it may provide for a particular, generic, expanded form of responsibility for fiscal

29 I.e. JL 2015, Item 613.

30 Cf. draft amendment consisting in introduction in the Criminal Code of invoice-related offences – Bill amending the Criminal Code Act and certain other laws of 12 July 2016; so-called 'augmented confiscation' – Bill amending the Criminal Code Act and certain other laws of 23 May 2016. Also, cf. the 'Fuel Package' – Act of 7 July 2016 'amending the Value-Added Tax Act and certain other laws' (JL 2016, Item 1052); Standard Audit File for Tax – Act of 9 September 2015 'amending the General Tax Regulations Act and certain other laws' (JL 2015, Item 1649).

offences and misdemeanours that would extend to entities that deal with business matters, the financials of collective entities in particular, under a legal regulation, decision of a competent authority, contract or agreement, or actual performance. This provision enables to extend the fiscal penal liability to natural persons for fiscal torts proving individual under PFPC. The point is, above all, about offences whose subjective-side features have been made more specific with use of terms such as taxpayer/taxable person, payer, resident, or importer. The editorial modification consists in replacement of the phrase "organisational unit without legal personality, whom the relevant separate regulations afford with legal capacity" by "organisational unit without legal personality". This modification will, in practice, enable to ascribe 'complete perpetration' also to individuals dealing with financial or economic/business affairs in civil-law partnerships. It has to be borne in mind, though, that such entities could have well been liable to prosecution within the confines provided under PFPC, considering the generic forms such as aiding (Art. 20, Para. 2, in conjunction with Art. 18, Para. 2 of the Criminal Code Act of 6 June 1997[31]) or accompliceship (Art. 9, Para. 2 PFPC). The above solution should be assessed in positive terms, whereas the provision in question will be adapted to the wording of its Criminal Code counterpart, i.e. Art. 308 PCC).

Art. 62, Para. 2 PFPC concerns formal acts (without an effect of 'underpayment of a civil liability' among the characteristic of the objective aspect). Hence, Art. 37, Para. 7 PFPC has hitherto remained non-applicable to it. It should be reminded at this point that in order to tighten up the responsibility of the perpetrators who committed causative acts consisting in issuance of empty invoices (owing to complete lack of action and lack of identity of the subjective party), there has been a progressing change in the interpretation consisting in qualification of such factual states as acts fulfilling the hypothesis worded in Art. 271 PCC (intellectual offence).

While referring to new types of intellectual and material falsity introduced in the regulations (Art. 270(a) and 271(a) PCC), which might, to a degree, be competitive to Art. 62, Para. 2 PFPC, it has to be pointed that unreliable invoice referred to in Art. 62, Para. 2 PFPC rests within the scope of "false

31 I.e. JL 2016, Item 1137, as amended; hereinafter, 'PCC'.

testimony/evidence with respect to circumstances of potential relevance to determination of the amount of a public liability", as per Art. 271(a) PCC. In this respect, the differences in the two provisions appear on the subjective side; insofar as the acts covered by the drafted Article 271(a) PCC may only be committed with direct intent, the fiscal tort also encompasses conceivable intent. These remarks do not, however, pertain to extraordinary aggravation of penalty, an instance of which may only be applicable in a deliberate form – in the direct intent. Furthermore, extraordinary aggravation in the event that an offence has been committed under Art. 62, Para. 2 PFPC will exclusively be limited to invoices relative to which the aggregate tax amount constitutes substantial property. This premise also coincides with Art. 271(a) PCC. The foregoing comment means that in case both draft amendments (Bills) are adopted in their present version, the causative acts consisting in issuing unreliable or 'empty' invoices will bear the attributes of Art. 271(a) PCC as well as Art. 62, Para. 2 PFPC as far as aggravation of penalty is concerned. Hence, the institution of ideal concurrence of offences/crimes as set out in Art. 8, Para. 1 PFPC shall apply, with the resultant each-time application of the relevant Criminal Code provision (under threat of a severer sanction, and thus, ousting the PFPC regulation), with the resulting complete inefficiency of PFPC's provisions.

A minor, though quite essential, modification is also the case with Art. 62, Para. 1 PFPC. The phrase "for discharge of the obligation/benefit" is to be deleted; as a result, the penalisation scope of the said regulation is to be extended also to behaviours consisting in defective performance of tasks of issuing and dispensing invoices. Let it be noted that, in the doctrine and in the judicature, the phrase "for the obligation/benefit discharged" has been the basic differentiating factor between the offence typified in Art. 62, Para. 2 PFPC and that of Art. 271 PCC. It has namely been accepted that the former extended to unreliable invoices (with the underlying actual discharge of a performance, the data specified in the invoice not being fully compliant with the reality), whereas the latter concerned 'empty' invoices. Elimination of the afore-quoted phrase may render interpretation of the above regulations more complicated. This notwithstanding, the provision

in question will certainly be concurrent with the drafter Articles 270(a) and 271(a) PCC.[32]

8 Conclusion

In summary, the existing legal solutions that aim at closing the loopholes in VAT can be classed into three groups:

- removal or change (amendment/modification) of regulations or provisions that enable or facilitate escape from taxation or the obtaining of reimbursement of the tax. No such solutions have been put into effect in the period under analysis;
- introduction of legal solutions aiming at detecting, or facilitating detection of tax fraud, escape from taxation, or obtaining undue tax reimbursements. Most of the changes launched in the period under analysis had such an objective in mind (items 2 to 6);
- introduction of new forms or increased repressiveness of the existing sanctions for tax fraud, illegal escape from taxation, and fraudulent obtaining of undue tax reimbursements (items 7 to 9).

The direct fiscal effect will only be brought about by the legal solutions specified in item 1, as they eliminate or restrict the possibility of not declaring any tax liabilities, having their amount reduced, or disclosing or increasing a disbursement of tax. For instance, a reduced list of goods and services whereto domestic reverse charge applies causes suppliers of such commodity to declare the output tax and the tax liability while not receiving tax reimbursements anymore.

32 Within the new structure, Art. 62 PFPC is to be as follows:
- Para. 1 is to specify a fiscal misdemeanour consisting in issuance of no invoice or bill, issuance of the same in a defective fashion, or refusal to dispense the same (penalty of fine – up to 180 daily rates);
- Para. 2 is to specify fiscal tort in the basic type, consisting in issuance of invoice or bill in an unreliable way; the perpetrator shall be subject to penalty of fine up to 720 daily rates, or to imprisonment for a time no lesser than noe (1) year, or both penalties combined;
- Para. 2(a) will specify the privileged type of the offence typified in Para. 2, consisting in issuance of an invoice or bill in an unreliable way, or in using such document in case that the tax amount, based on the invoices, is of a low value. The perpetrator will, in such a case, be subject to a penalty of fine of up to 270 daily rates or to imprisonment, or both, combined.

The solutions listed in item 2 increase the budget revenue with the tax in question only to a slight extent, though they may objectively increase the amount of tax liabilities disclosed in the tax by means of:

- issuing decisions determining the tax arrears;
- voluntary adjustments of tax returns, inspired by inspection actions.

The actual fiscal efficiency of these actions, particularly those specified in item (a), is low – with some 5 per cent of due amounts, on average. A slightly better fiscal effect appears with quasi-voluntary adjustments or returns whose submittal results from a legitimate concern that the occurring irregularities might be discovered, although there is no complete data on the amounts. Submittal of adjustments is often driven by one's willingness to avoid fiscal penal responsibility of those responsible, rather than a willingness to make up for the disclosed tax arrears.

The solutions specified in item 2 mainly aim at focusing inspection activities on the entities which may be legitimately suspected of tax fraud, illegal escape from taxation or fraudulent obtaining of undue tax reimbursements. Taking into account the fact that taxpayers submitting returns form a population of some 1,8 million entities, the number of taxpayers only performing tax-exempt actions remaining unknown (there is no register in place; probably, there are some 1,5 milion actual entrepreneurs and an even larger group of entities being in fact members of staff, though they do issue invoices or bills). The number of those submitting returns with tax reimbursement option is in excess of 1,3 Mio. per annum. Hence, sovereign actions should exclusively be focused on significant cases, for efficient control may only extend, on a yearly basis, to a dozen thousand entities, at the most. If the selection can be effected, with use of instruments monitoring tax settlements of taxpayers, the formal fiscal efficiency of controlling / inspection actions will increase, which may bring about a real fiscal effect. Hitherto, no sufficiently selective solutions have been developed yet which would have enabled to compile a list of risked transactions and entities that would correspond with the VAT specification. Some hope may be attached

to the obligation to provide the records kept for VAT purposes [JPK_VAT]; however, the concept launched in Poland has certain obvious flaws to it, since:

- not all the invoices issued for purposes of this particular tax are inventoried by taxpayers;
- forged invoices are, as a rule, carefully entered in tax records, as only then one may fraudulently obtain a deduction or reimbursement.

The base instruments that could be used for the purposes of eliminating risked transactions and entities include the central and verified list of taxpayers and the central register of invoices issued. In spite of multiple announcements, no such solutions have been put into practice from 2019 onwards.

The solutions enumerated in item 3 may imply direct fiscal effect, for the sanctions are of the tax type and thus consist in repressive increasing of tax liabilities or adjudication of additional tax liabilities. Yet, direct effects of fiscal use of these instruments are not-quite-significant, and this is not the way along which fiscal efficiency of the tax in question, or any other tax, would be increased. The deterring effect is of crucial importance: these sanctions may bear it, in line with the proportionality principle, in relation to the benefits potentially achievable through escape from the tax and, especially, through fraudulent obtaining of undue tax reimbursements. It is undisputable that the changes discussed in item 7 are critical, since a proportional punishment, related to benefits obtained resulting from abuses in VAT, has been introduced there. How Clarke and Fox (2015) mentioned tax expenditures hide the costs of government spending.

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Composite Transactions in Light of the Case Law of the Court of Justice we European Union and the Supreme Administrative Court

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Abstract

This contribution deals with the notion of the composite transactions in the field of VAT. Such a notion does not have its normative definition in the EU legislation. It is the case law of Court of Justice of European Union (hereinafter "CJEU") that defined the conditions when, as an exemption from the general rule, multiple supplies are to be a treated as a single supply for VAT purposes. The main aim of the contribution is to confirm the hypothesis that the lack of normative definition of notion of the composite transactions the application of the guidance of the CJEU by the national courts raises some fundamental questions and can lead to a practical problems when dealing with VAT cases on national level. The research was conducted by using the dogmatic and comparative method. Those methods were used to define the notion of composite transaction taking into account the guidelines presented both on EU level and the national level. Analysis of the those aspects lead to the final conclusions that there is a need to define this notion in both European and national law in order to overcome the difficulties in applying such a notion to VAT cases.

Keywords: Tax; Law; Value Added Tax; Composite Transactions; Case Law of Court of Justice of European Union; Case Law of Supreme Administrative Court.

JEL Classification: K34.

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1 Introduction

This contribution deals with the notion of the composite transactions in the field of VAT. Such a notion does not have its normative definition in the EU legislation. It is the case law of Court of Justice of European Union (hereinafter "CJEU") that defined the conditions when, as an exemption from the general rule, multiple supplies are to be a treated as a single supply for VAT purposes. The main aim of the contribution is to confirm or disapprove the hypothesis that the lack of normative definition of notion of the composite transactions the application of the guidance of the CJEU by the national courts raises some fundamental questions and can lead to a practical problems when dealing with VAT cases on national level. Liška (2018) noticed that nowadays it seems that the preclusion period is only or substantive obstacle to the application of full neutrality of value added tax.

The potential difficulties in resolving such cases are also raised in the national jurisprudence (Bartosiewicz, 2013: 277). Doubts concern, firstly, the qualification of a given transaction as a single composite transaction, or rather as multiple transactions. In the same context, it is unclear when a given group of transactions comprises one taxable item, and when it comprises multiple taxable items. Secondly, there are doubts arising from the manner of taxation of a composite transaction containing multiple and frequently diverse elements.

It is also pointed out that in the second decade of the 21st century, economic reality is replete with numerous and frequently complicated transactions. There are few commercial entities that presently offer goods or services of a uniform character. Transactions are generally composed of several types of activities, the proper qualification of which is important from the perspective of rules governing value added tax. The appropriate assignment of the given activities of a taxpayer as the supply of goods or services is important in determining the rate of the tax, as well as the possibility to apply exemptions (Bzowska, 2015: 9).

The contribution will provide answers to the following fundamental questions:

- Has the CJEU in its case law elaborated the notion of composite transactions, which is not a normative concept?

- In the case law of the CJEU, when is a transaction considered a composite transaction, and when is the separate taxation of services applied?
- In interpretations of the provisions of tax law, does the case law of the Supreme Administrative Court (hereinafter: "SAC") employ the doctrine of composite transactions, and do the judgments of the CJEU exert a significant impact on the case law of administrative courts in Poland?
- Can composite transactions be used to engage in evasion of tax law?

Answers to those questions will be provided taking into account the guidance given by the CJEU and the practical application of such guidance by the SAC. The research was conducted by using the dogmatic and comparative method. Those methods were used to define the notion of composite transaction taking into account the guidelines presented both on EU level and the national level.

Firstly the notion of the composite transaction is defined. Then the case law of CJEU on the conditions and interpretation of such notion in a context of Polish prejudicial question is presented. Thirdly, the case law of SAC is discussed as an example of applying the notion of composite transactions on the national level. Finally the notion of composite transactions is discussed in a context of the possible evasion of tax.

Analysis of the those aspects lead to the final conclusions that there is a need to define this notion in both European and national law in order to overcome the difficulties in applying such a notion to VAT cases.

2 The notion of composite transactions

There is no normative definition of the notion of composite transactions. None can be found in Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (OJ L 347: 1, hereinafter "VAT Directive"), nor in the Polish Value Added Tax Act of 11 March 2005 (OJ L 2011, No. 177, item 1054 as amended, hereinafter "VAT Act"). Thus, jurisprudence can have a significant role to play.

An attempt at defining the borders of the notion under analysis was made by the CJEU)in its judgment of 27 September 2012 (CJEU: case C-392/11 *Field Fisher Waterhouse LLP* v. *Commissioners for Her Majesty's Revenue and Customs*) using the existing case law. In this ruling, it was indicated that for the purposes of VAT, each supply should usually be considered separate and independent, as results from Art. 1(2) second paragraph VAT Directive (see similar CJEU judgments in cases: C-111/05 *Aktiebolaget NN*, para 22; C-461/08 *Don Bosco Onroerend Goed*, para 35; case C-276/09 *Everything Everywhere*, para 21 – thesis 14). Within this scope, the Court ruled that one supply exists when at least two elements or two activities performed by the taxpayer are so closely linked that they objectively comprise one inseparable transaction, whose division would be artificial (see similarly judgment of 27 October 2005, (CJEU: case C-41/04, *Levob Verzekeringen and OV Bank*, para 22; case C-276/09 *Everything Everywhere*, paras 24 and 25).

Furthermore, it is also the case that if one or more supplies should be considered the principal supply, while the remaining one or ones constitute ancillary services, they are treated from the tax perspective the same as the primary supplies. In particular, a transaction should be acknowledged as ancillary to the principal if it does not constitute the client's primary objective, but rather serves to make the best use of the principle service supplied (see CJEU judgments in cases: C-349/96 *Card Protection Plan*, para 30; C-425/06 *Part Service*, para 52; joined cases C-497/09, C-499/09, C-501/09 i C-502/09 *Bog et al.*, para 54).

Taking into account two circumstances – firstly, that each supply should usually be considered separate and independent, and secondly, that a transaction comprised of one supply in the economic aspect should not be artificially divided in order to avoid negatively impacting the functionality of the VAT system; it is necessary to seek elements characteristic of the reviewed activity in order to determine whether a given transaction consists of several separate primary supplies, or is rather a single composite transaction (see similarly CJEU cases: C-349/06 *Card Protection Plan*, para 29; C-41/04 *Levob Verzekeringen and OV Bank*, para 20; C-111/05 *Aktiebolaget NN*, para 22; C-276/09 *Everything Everywhere*, p 21 and 22).

Nevertheless, within the framework of cooperation established under Art. 267 TFEU, national courts are responsible for determining whether in a given case the taxpayer is providing a single service, as well as engaging in a comprehensive final assessment of the facts of the case within that scope (see similarly CJEU: case C-349/06 *Card Protection Plan*, para 32; case: C-425/06 *Part Service*, para 54; joined cases C-497/09, C-499/09, C-501/09 and C-502/09 *Bog et al.*, para 55; case C-117/11, *Purple Parking and Airparks Services*, para 32). However, the CJEU should supply national courts with significant guidance concerning interpretation of EU law which can applied when adjudicating on matters before those courts (CJEU: case: C-41/04, *Levob Verzekeringen and OV Bank*, para 23 – thesis 20 judgment).

Despite these introductory considerations, the CJEU arrived at the surprising conclusion that interpretation of the VAT Directive should lead to the conclusion that the leasing of real property and associated provision of services, such as those comprising the subject matter before the national court, can comprise a single service from the perspective of VAT. In this respect, the possibility given by contract to the lessor to dissolve the contract in the event the lessee fails to remit additional payments for the lease indicates the presence of a single supply, although it is not definitively a determining factor when assessing the presence of such a transaction. However, the circumstance that the provisions of services such as those constituting the subject matter before the national court may, as a rule, be performed by a third party does not allow for the conclusion that those supplies cannot, in the circumstances of those proceedings, constitute a single supply. The national court is to determine in the light of the instructions concerning interpretation issued by the Court in that ruling, as well as taking into account the particular circumstances of the case at hand, whether the transactions under consideration are linked to such an extent that they should be considered one single transaction in the form of rental of real property.

3 CJEU case law concerning composite transactions in Polish cases

The CJEU has twice ruled in cases involving Poland and composite transactions.

In the first judgment, of 17 January 2013 (CJEU: case C224/11 *BGŻ Leasing*), it was held that the supply of insurance services for a leased item and the supply of the leasing services themselves must, in principal, be regarded as distinct and independents supplies of services for VAT purposes. It is for the referring court to determine whether, having regard to the specific circumstances of the case in the main proceedings, the transactions concerned are so closely linked that they must be regarded as constituting a single supply or whether, to the contrary, they constitute independent services. In the context of leasing, a transaction consisting in re-invoicing the exact cost of insurance for the leased item, like that at issue in the main proceedings, constitutes an insurance transaction within the meaning of Article 135(1)(a) of the VAT.

In this judgment it was essentially decided that insurance of a leased item should be treated as a separate service, not leaving the national court with discretion in that issue.

A procedural problem thus arose in the application of Art. 269 of the Act on proceedings before administrative courts.

Indeed, prior to the CJEU's judgment, a resolution of a panel of seven judges of 8 November 2010 (Supreme Administrative Court, I FPS 3/10), the SAC expressed the view that in light of Art. 29(1) of the VAT Act, according to the law in effect in 2006, an entity offering leasing services should include within the tax base for those services costs of insuring the leased item.

In its judgment of 27 June 2013 (Supreme Administrative Court, FSK 720/13), the view was expressed that in the case of a judgment issued by the CJEU in response to an application for a preliminary ruling, the application of the procedure set out in Art. 269(1) of the Act on proceedings before administrative courts is unnecessary in order to achieve compliance of the interpretation employed with European law.

In a dissenting opinion to this judgment, the present author took the position that in the case at hand, it was necessary to first activate the statutory procedure set out in Art. 269(1) APBAC, in order to achieve an interpretation compliant with EU law and to eliminate a resolution inconsistent with EU law. This is a consequence of the principle of procedural autonomy of states and certainty in the application of the law.

The change to the position of the SAC following the CJEU judgment in favour of the taxpayer had further implications. Leasing companies revised incorrect tax filings and applied for refunds of overpayment of VAT. Unfortunately, they did so following the five-year limitation period for applications for refund of overpayment. Thus, a serious legal question arose of whether the expiration of the limitation period, despite the judgment of the CJEU, made it impossible to pursue the refund. As a result of a motion for a preliminary ruling by the SAC, the CJEU addressed this question in its judgment of 20 December 2017 (CJEU: case C500/16 *Caterpillar Financial Services*), in which it ruled that the principles of equivalence and effectiveness, read in the light of Article 4(3) TEU, must be interpreted as not precluding national legislation, such as that at issue in the main proceedings, which allows a request for a refund of an overpayment of VAT to be refused where that request was submitted by the taxable person after the expiry of the five-year limitation period, although it follows from a judgment of the Court, delivered after the expiry of that period, that the payment of the VAT which is the subject of that request for a refund was not payable.

The second judgment of the CJEU in a Polish case was handed down on 16 April 2015, (CJEU: case C-42/14, *Wojskowa Agencja Mieszkaniowa*). In this ruling, it was held that Articles 14(1), 15(1) and 24(1) of the VAT Directive must be interpreted as meaning that, in the context of the letting of immovable property, the provision of electricity, heating and water and refuse collection, provided by third-party suppliers for the tenant directly using those goods and services must be regarded as being supplied by the landlord where he has concluded agreements for the provision of those supplies and simply passes on the costs thereof to the tenant. Furthermore, it was held that the VAT Directive must be interpreted as meaning that the letting of immovable property and the provision of water, electricity and heating as well as refuse collection accompanying that letting must, in principle, be regarded as constituting several distinct and independent supplies which need to be assessed separately for VAT purposes, unless the elements of the transaction, including those indicating the economic reason for concluding the contract, are so closely linked that they form, objectively, a single, indivisible economic supply which it would be artificial to split.

It is for the national court to make the necessary assessments taking into account all the circumstances of the letting and the accompanying supplies and, in particular, the content of the agreement itself.

In the judgment it was emphasised that it essentially depends on the civil law contract associated with the leasing of premises whether a given activity comprises part of a composite service, or whether the activities can be split and taxed differently. This is a novelty in the jurisprudence (alongside good and bad faith, and evasion of the law), as it does not come directly from legal provisions. And thus, the taxpayer himself can shape the extent of the tax due with the help of certain provisions of a civil law contract.

Following the interpretation contained in the above judgment, the Court in its judgment of 25 August 2015 (Supreme Administrative Court, I FSK 1672/13) expressed the view that the Minister of Finance, in contrast to the position it took in the interpretation appealed against, should take into account that the supply of electrical energy, heat power and water as provided by the lessor alongside the primary service of rental comprise separate services from the service of rental, to the extent that the lessee has the possibility of choosing to use those goods, and the parties determine in their agreement that the lessee will settle the costs of rental and monies due foot other goods separately, based on individual usage amounts.

4 Case law of the Supreme Administrative Court concerning composite transactions

In its judgment of 18 December 2012 (Supreme Administrative Court: I FSK 339/12,), the SAC held that ICT services associated with service of payment cards for a bank on the basis of Art. 43(13) in conjunction with Art. 43(1)(40) VAT Act are subject to exemption from VAT. The second part was adopted of the definition contained in the judgment of the CJEU (CJEU: case C-392/11 *Field Fisher Waterhouse LLP*), that ICT services are ancillary to financial and banking services, and they are difficult from the perspective of the consumer to split, as card payment is perceived first and foremost as a financial service.

In another judgment of 25 February 2015 (Supreme Administrative Court: I FSK 1783/13) the Court held that services provides by a party consisting in reservation of a taxi is, from the economic perspective, a service inextricably connected with the taxi service. In the period 2007–2009, in the vast majority of cases, to order a taxi and use the taxi service it was first necessary to reserve it by telephone. For consumers, this contact with a taxpayer led to the realisation of a service. Direct telephone contact by the consumer with the taxi driver cannot be considered a separate service. Treating the service under dispute as a separate service would seem artificial and contrary to the pro-EU interpretation as presented and as results from the previously cited judgments of the CJEU. For this reason, it should be considered appropriate to rule in favour of the cassation application which claimed violation of Art. 5(1), Art. 8(1) and Art. 41(13 and 14) of the VAT Act within such scope as the service provided by the complainant was not ruled to be a composite service associated with the taxi service.

In its resolution of 24 June 2013 (Supreme Administrative Court, I FPS 2/13), the SAC took the position that according to the law in effect from 1 January 2011, composite services consisting in the design, adaptation and assembly of components in a manner that, together with construction elements of a building or parts thereof comprises a furniture installation, made in buildings comprising a construction project encompassed by a social housing program, constitutes a modernisation service subject to a lowered VAT rate based on Art. 41(12) in conjunction with Art. 2 of the VAT Act.

Numerous court disputes have concerned the provision of medical services within the context of composite transactions. In its judgment of 1 June 2011 (Supreme Administrative Court: I FSK 869/10), the SAC indicated that there was no definition in Polish or EU law referring to VAT. It is necessary to analyse in each case, based on specific factual circumstances, the nature of a series of activities linked to one another. The case law of the Court of Justice of the European Union does contain certain general indications helpful in making such rulings. The supply of medical equipment in the form of adaptation as indicated by the taxpayer of the premises where the equipment will be used, if the supplier did not demonstrate that the supply and the performed services are linked with one another in such a manner

that their separation would be artificial, thereby weakening the functionality of the VAT system, even if each of the services provided retains its usability from the perspective of the needs of the hospital as an average consumer. This does not mean that those services are inextricably linked economically. A composite service is the supply of equipment and its assembly, that is a situation in which the performance of one transaction is impossible without the existence of the other transaction. It is necessary to separate any link of particular services from such a link between them that determines they must be regarded as one composite transaction. It is not permissible to adopt such a classification of services solely on the basis of the subjective element, placing emphasis on the indication of the service satisfying the primary need of the customer, while acknowledging that the remaining services are in any manner at all ancillary to than need, without analysis of the other aspect of such services. While from the perspective of the hospital as the purchaser of the equipment the execution of construction work to perform adaptations by the supplier of medical equipment is doubtlessly beneficial and desirable, it cannot be considered that such work is to closely coupled with the delivery of that equipment that together with its delivery it constitutes one service, assuming that from the perspective of the needs of the hospital it is of such a universal nature that the performed services can be applied to medical equipment other than that actually delivered. In combining particular deliveries or services provided into one transaction, it must not be forgotten that the statutory principle is separability and independence of particular deliveries/services performed. It is thus an exception to the rule to hold that separate services in fact constitute a single composite transaction.

A similar view was expressed by the Supreme Administrative Court in its judgments of 28 June 2011 (Supreme Administrative Court: I FSK 958/10), 27 April 2012 (Supreme Administrative Court: I FSK 974/11), 6 June 2012 (Supreme Administrative Court: I FSK 1374/11), 19 October 2018 (Supreme Administrative Court: I FSK 1881/16), 30 October 2014 (Supreme Administrative Court: I FSK 1578/13).

Another issue taken up by administrative courts in Poland was VAT taxation of the free handing out of goods done as part of the performance

of a composite marketing service. In its judgment of 26 August 2015 (Supreme Administrative Court: I FSK 1340/13) the SAC held that the determination of the provision by a taxpayer of a composite marketing service, encompassing, inter alia, the handing out of products and performance of services to the benefit of principals, may be made when the recipient of such a composite service is the principal on whose behalf the service is provided. The company that provides the promotional service on behalf of a pharmaceutical concern must pay VAT on gadgets given to doctors.

In another judgment of 21 April 2015 (Supreme Administrative Court: I FSK 579/14) the SAC ruled that in the view of the Court, nothing stands in the way of splitting payment into two elements, each of which would account for a separate service. Determining payment in the portion encompassing the value of rewards given to third parties was possible as the complainant was also the party that acquired them. A separate issue, however, was the qualification of the additional costs associated with the presentation of the rewards to third parties. These costs, as results from the CJEU judgment (CJEU: joined cases C-53/09 and C-55/09 *Loyalty Management UK et al.*), could have comprised a portion of the remuneration for the performance of the marketing service (…) the marketing service and the purchase and transfer to third parties of the rewards are not so closely coupled that they objectively comprise one indivisible economic transaction whose splitting would be artificial as understood by the jurisprudence of the CJEU.

A similar view was expressed regarding the qualification of marketing services by the SAC in its judgment of 15 October 2014 (Supreme Administrative Court: I FSK 1443/13) and of 13 February 2018 (Supreme Administrative Court: I FSK 645/16).

It results from analysis of the SAC case law that it has accounted in its jurisprudence for the interpretation of tax law provisions given by the CJEU.

5 Evasion of the law and composite transactions

The provision of composite services has been used in individual cases to evade the law. This has consisted *inter alia* in how, with regard to the provision of services with multiple tax rates, e.g. 8 % and 23 %, commercial

entities engaged in gastronomic activity involving a restaurant that offered under promotional auspices the sale of packages containing a beer and breadsticks, vodka and a lemon, and coffee or tea with a cookie; what is of significance here is that the restaurant registered the sale as the sale of two goods subject to VAT at different rates – at the primary rate of 23 % (beer, vodka, coffee, tea), and at the 8 % rate for the sale of breadsticks, lemon and cookies (which were assigned different unit prices in different packages), thereby reducing for marketing purposes the tax base of goods subject to the higher rate and simultaneously increasing the tax base for goods subject to the lower rate. In its judgment of 9 May 2017 (Voivodhip Administrative Court in Lublin: I SA/Lu 166/17), the court indicated the manipulation of the VAT tax base in the sale of goods in package form by artificially inflating the price of goods subject to a lower VAT rate while simultaneously decreasing the price of goods subject to the primary VAT rate in order to achieve tax benefits was an evasion of the law as set out in Art. 5(4 and 5) of the VAT Act. In determining the appropriate VAT rate for taxation of the package, it is necessary to first determine what product constituted the primary transaction and which was ancillary, then adopt for the entirety of the transaction the tax rate set out in Art. 41 VAT Act.

In a positive case-comment to that judgment, M. Fedorowicz (Fedorowicz, 2016: 116) indicated that the complainant, by setting the price of particular elements of the package, essentially engaged in manipulation of the tax base in the sale of goods subject to various VAT rates, thereby achieving unjustified tax benefits, and the objective of the setting of prices was to reduce the amount of tax due. In both the judgment of 26 May 2017 (Supreme Administrative Court: I FSK 1944/15) and the case comment to the judgment it is clear that the questioned transactions, despite fulfilling the formal premises, effected the attaining of a tax benefit contradictory to the objective of the VAT Act. Furthermore, as can be deduced from the CJEU case law, it is considered that this type of activity constitutes evasion. Transactions which when engaged in constitute an evasion should be redefined in such a manner as to recreate the situation that would have existed if the transactions constituting the evasion had not taken place; this may and should comprise a certain model for reconstruction in situations

involving review of the existence of an evasion clause. However, it should be emphasised that on the basis of the VAT tax law, the tax authorities are fully entitled to apply the evasion of law clause, as this rule is grounded in the general system, and also indirectly in the principle of VAT neutrality.

A similar view was expressed regarding the potential for evasion of tax law in composite transactions concerning the sale of packages encompassing goods subject to different VAT rates by B. Rogowska-Rajda and T. Tratkiewicz, (Rogowska-Rajda et al., 2018).

In a judgment of 26 May 2017 (Supreme Administrative Court: I FSK 1767/15) the SAC indicated that separating a restaurant service into the service portion and the sale portion linked with the sale of products (e.g. coffee) would lead to the artificial splitting of the restaurant service. Indeed, it results from the essence of that type of service that it is provided in a restaurant, and its purpose is not only ensuring the comfortable consumption of food and drink, but also the sale of products in precisely those conditions. By the same token, the splitting of a composite restaurant service into *stricte* services and the supply of products would be an artificial and irrational act. It is thus possible to apply the reduced 8 % rate to the provision of gastronomic services, but at the same time with the exclusion of the possibility to apply that rate to cases involving the sale of goods including coffee, tea and beverages, regardless of whether they constitute an ancillary element to the gastronomic service or not.

In another judgment of 2 March 2016 (Supreme Administrative Court: I FSK 1672/14) the SAC held that there are no grounds for services encompassing the preparation and service of beverages to be separated into a "service portion" and "sale of goods (beverage) portion", as this constitutes – within the context of services associated with food – a uniform act of provision of the service of preparing and serving beverages which – having as its subject matter the beverages listed in points 1) to 5) from item 7 of Attachment no. 1 to the Regulation of the Minister of Finance of 4 April 2011 on the implementation of some provisions of the Act on value added tax – is subject to the primary tax rate (23 %).

In another judgment of 20 April 2017 (Supreme Administrative Court: I FSK 1982/15), the SAC also took up the issue of taxation of restaurants. In this

ruling, the court indicated that the provisions of Art. 3(1)(1) in conjunction with item 7 of the Attachment to the Regulation of 23 December 2013 on goods and services for which the rate of value added tax is reduced and the conditions for applying reduced tax rates allows for the taxation of restaurant services (associated with feeding) at the lower rate of 8 %, but only with respect to the portion that does not correspond with the sale within this service of goods listed in item 7 of Attachment no. 1 to this Regulation.

The Supreme Administrative Court has also taken up the issue of composite transactions in the context of hotel services. In its judgment of 6 December 2013 (Supreme Administrative Court: I FSK 1758/12) the SAC indicated that accommodation with breakfast is a primary service of a composite nature. A single VAT rate is applicable to them. Other ancillary services, such as spa treatments or dinner, are separate transactions. Whether we are dealing with one composite service or multiple separate ones is determined by whether they comprise an entirety in the commercial sense. However, the mere will of the parties cannot determine the scope of VAT taxation.

Composite transactions can be exploited through the differentiation of tax rates for evasion of the law, but then can be called into question based on the case law and jurisprudence developed by the CJEU.

6 Conclusions

In the second decade of the 21st century, civilizational development and new technologies will lead to the increasingly frequent appearance of composite transactions in commercial dealings.

There is no normative definition of composite transactions, which causes difficulties in interpreting the tax base and adopting the appropriate tax rate.

In its case law, the CJEU has attempted to define the notion of composite services through the general principle that particular services should be split under the condition that this is not artificial, and does not hinder the functioning of value added tax. The CJEU has indicated that one service is provided when at least two elements or at least two activities performed by the taxpayer are so closely linked that they objectively constitute only

one inseparable economic transaction, whose splitting would be artificial. Furthermore, it is also the case that if one or several transactions should be considered the primary service, while the other(s) constitute an ancillary service(s), they are treated from the tax law perspective as the primary service. In particular, a transaction should be considered ancillary to the primary transaction if it does not constitute a purpose in and of itself for the client, but rather serves to maximise enjoyment of the primary service.

Assessment of whether a transaction is of a composite nature should be done by the national courts. Yet the CJEU did not allow for this in the case C-224/11 *BGŻ Leasing*.

One new element is that in respect of lease of premises and payments for utilities, it is possible to separate services – *de facto* determining the amount of the tax obligation – depending on the content of a civil law agreement. The construction of composite transactions can be used to evade tax law.

From analysis of the case law of the CJEU and SAC, we can conclude that the absence of a normative definition of composite transactions leads to numerous tax disputes. It is thus necessary to propose the initiation of legislative work intended to define this notion in both European and national law.

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Indirect Taxes in EU Law – Recent Developments after the Crisis
(Considerations on Current VAT Reform)

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Abstract

This contribution deals with the current VAT reform in the EU. It examines two problems: The new system of taxation of goods in intra-Union trade (the final principle of destination state but with a new obligation to levy the tax by the supplier in the state of origin) and, secondly, the liberalisation of reduced VAT rates. The main aim of the reform is to combat fraud and to meet legitimate needs of member states. The conclusion confirms that apart from minor problems the reform will be welcomed by member states as a progressive development of the VAT system.

Keywords: Value Added Tax; Reduced Rates; EU VAT Reform; Intra-Union Supply of Goods; EU Cross-Border Trade; Tax Fraud.

JEL Classification: K34.

1 Introductory notes

The aim of the present article is to explain and analyse recent developments in the VAT regulation in the intra-Union trade, which brings considerable changes comparing to the present state. It was first presented by the European Commission in 2016 as Action Plan on VAT – Towards a single VAT area (European Commission, 2016). We shall concentrate on the value added tax only, since it is the most important tax related to the EU internal market. Two principal problems have been selected and will be examined:

- VAT taxation in the EU cross-border trade,
- redesign of VAT reduced rates as a consequence of point a).

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The aim of the analysis is to prove that the reform carried out will be welcomed by member states and will ensure better functioning of the VAT system in the EU internal market. Methods used to reach that goal are description, analysis and synthesis.

Since the VAT reform is very recent and still ongoing, there are not yet many specialised sources analyzing it. Main resources in this field are above all EU official documents and brief reactions of practicians published on the web.

2 Value Added Tax in the EU Internal Market

Let us examine first why the value added tax is the concern of the European union. Any goods or services are subject to the VAT as a national tax. In the same time, the goods and services have to circulate freely in the EU internal market, regardless the borders between member states. For this reason the VAT has to be harmonized on the Union level.

Free movement of goods and services requires the abolition of all administrative and fiscal obstacles of trade. One of them could be potentially the VAT, since each member state has its own national VAT system. This makes the necessity of the harmonization of VAT in order to establish a smooth system of taxing the cross-border trade of products and services.

Another problem that we shall elaborate is that of TVA rates. It is certain that the unification or at least the harmonization of rates is impossible, since every state considers them crucially important for the income of its national budget and for the social policy and accordingly is not willing to accept any external influence for their determination.

2.1 VAT and cross-border transactions – initial state at the early Internal Market (1991)

Cross-border transactions seem to be simple from the administrative point of view – the trade is free without any custom taxes or other limitations. Nevertheless, the products (including services) are taxed in the member state of origin as any other products. In addition to that, the said products are taxed in the country of destination just as any other product of that

country. The essential rule there is that of the prohibition of discrimination of imported products, which is the basic principle of the EU internal market concerning the free movement of goods. In fact, it is necessary to prevent such a double taxation. The products being subject of the trade between member states cannot be taxed twice, otherwise their price would turn off customers because being too high.

In the transborder trade the main problem is the coexistence of two different tax systems of countries whose businesses are operating across the borders. Delivered products are to be taxed by the VAT only in one of the two countries.[2] Both alternatives have advantages and disadvantages.

Final taxation in the ***country of origin*** means that the goods do not cross the border untaxed. Thus it eliminates the most common occasion for a potential fraud – selling the untaxed goods back in the country of origin or in another country. This would be a strong advantage, since the dimensions of tax fraud is now in the intra-Union trade reaching distressing proportions. Another advantage is that this method excludes any discrimination between imported and local goods, since both are subject to the taxation using automatically the same rate.

Unfortunately, there is a decisive disadvantage: the tax constitutes an integral part of the final price of the goods. The price of goods produced in countries with high VAT rate would be more expensive than those produced in countries with low rate. This would affect the flow of goods – relatively cheap goods from countries with low VAT rate would be more competitive. This would be absolutely contrary to the concept of the EU internal market. The only remedy could be the unification of VAT rates in all EU member countries, which is an unrealistic idea.

Taxation in the ***country of importation (destination)*** is based on the fact that the goods cross the border untaxed and the VAT is charged only after the importation using the rate of importing state. The advantage is that it does not matter what VAT rate is used by the importing state, the result is always same. Imported goods must be charged with the same rate as local

2 Council Directive 91/680/EEC of 16 December 1991 supplementing the common system of value added tax and amending Directive 77/388/EEC with a view to the abolition of fiscal frontiers.

products. Nevertheless, there are two disadvantages of that alternative. The first is the possibility of the potential discrimination of imported goods by applying different taxation conditions for them. The second is more serious: The movement of untaxed goods before the importation leads to tax frauds, when the goods are not taxed in the destination country and are sold elsewhere.

The current state is based on the taxation of the goods in the destination country, since the principle of the country of origin is not acceptable for the EU internal market. The same principle is being used generally in the international trade outside the EU. VAT charged in the country of origin is refunded when the goods leave the territory of that country and it is subject to taxation in the destination country (Aujean, 2012–13: 140 seq., Lapalus, 2014: 25 seq.)

The European Commission originally did not accept the destination country principle for the taxation as a definitive solution, but only as a temporary one. There were two reasons:

1. The cross-border trade is, from the administrative and civil law view, a unique transaction, normally not complicated. However, it is subject to two different taxations: In the state of origin, the VAT charged for the exporting goods must be refunded and in the destination state it is charged again and paid by the final customer. There is no single "VAT operation", but there are two, in two different member states. The Commission would be in favour of a single VAT operation covering the transaction of goods from the production to the consumption in another member state.
2. Second concern of the Commission is the tax fraud abusing the fact that the goods leave the state of origin untaxed.

Consequently the Commission considered in the time of establishment of the internal market in 1991 the destination state principle as a transitional solution, that will be replaced sometimes in the future by the ultimate state of origin principle. Nevertheless, to rely on the unification of VAT rates in the whole Union was not realistic. For that reason the Commission did not insist on the change.

2.2 VAT fraud

The most frequent fraud is the carousel fraud, when some enterprises buy untaxed goods and resell them with tax, but never pay the tax so collected. For comments see Aujean, 2012–13: 140.

The carousel fraud is described also by Duffy and O'Donovan, 2017: 128 in this way: "The fraudsters manipulate the cross-border and domestic VAT rules to create a situation where they can purchase goods without payment of VAT and sell them on with VAT to innocent traders." The tax fraud may have many forms, it may be even unintentional (Šimonová, 2018: 127).

Another example of a VAT fraud is the following one: The goods are produced in the state of origin using the 23 % VAT rate. Then the parties just ***simulate the exportation*** of goods to the destination country using the rate of 18 %. In both countries the goods will be declared. The VAT in the first state will be refunded (23 %) and in the second state it will be paid (18 %). The difference is 5 %–the profit of fraudsters.

It is clear that the development in recent years required a vigorous moving ahead. The VAT fraud in the intra-Union trade has grown to such an extent that it became intolerable. It is evaluated to 150 000 000 000 € a year (for the whole EU). This was the principal impulse for the Commission to elaborate a substantive reform of the EU VAT system that would not only limit fraud but also make the functioning of the VAT system at the EU internal market more smooth. The capital idea is to merge the two VAT operations into one and arrange that goods will leave the territory of the state of origin only after the VAT is charged. Taxed goods in the trade will be less attractive for tax fraudsters than untaxed ones.

2.3 2016 VAT Reform for the intra-Union trade

The present temporary system is based on the taxation in the destination country. This is the only possible alternative because of the diversity of VAT rates in different member countries. It means that the ultimate system established by the Commission must be based on the destination country as well regardless the intention of the Commission for, sometimes, the taxation in the country of origin. The VAT must then come under the revenue

of national budget of the destination country. However, it could be levied at the very beginning of the cross-border movement of the traded goods, i.e. in the state of their origin. This new concept represents an ingenious merger of two categoric requirements: the VAT should be charged by the state of destination but in the same time levied by the supplier in the state of origin, i.e. before the goods leaves its territory. The taxation of goods exported to another Member State will be identical to the taxation of goods not leaving the territory of the state of origin. The only difference will be the rates applied – for the exportation the rate of the destinantion country will be used. Shortly speaking, instead of two taxable events in two different Member States there will be a single tax event named ***intra-Union supply of goods***. Basic EU documents are (European Commission 2016, 2017, 2018).

The characteristics of the new system will be:

- no distinction between domestic and intra-Union transactions,
- no need for different obligations for intra-Union transactions (like listing intra-Union transactions,
- no need to prove the transport of goods out of the country of the supplier. (Aujean, 2012–13: 141).

This complex framework requires to comment on at least four new basic problems.

1. The VAT will be charged only once and definitively in the country of origin of the goods and then not refund. The goods will be taxed from the moment of their production and will cross the border already taxed. As soon as delivered to the destination country, they will not be taxed again. It means that such a practice will eliminate at least one category of tax frauds – those based on the abuse of the fact that the goods moving across the border are untaxed (for instance the dissimulation of importation and subsequent selling of untaxed goods in other than destination country).
2. Second note relates to VAT rates. Traded goods should be taxed by the rate in force in the destination state, not the state of origin. It means that the VAT in the state of origin has to be charged at the rates of the destination state. This represents an interesting legal problem – it is supposed that the supplier, and consequently the tax

administration of the country of origin will apply tax laws of another (destination) country. This is very unusual. Contrary to the private law, public law is too closely related to the state and normally public law rules cannot be applicable in another state. This innovation in the taxation of cross-border deliveries of goods is thus in the same time an innovation in the extraterritorial application of tax law rules in the opposite sense – not the application of internal law on the foreign territory, but of foreign law on the national territory. In some cases it could be rather difficult to identify applicable rates especially in cases of multiple reduced rates effective in the delivery state.

3. The VAT levied in the state of origin by its tax administration belongs to the destination state. Consequently, it must be then transferred to the tax administration of that latter state. Shortly speaking, the VAT will be charged by the destination state, but just technically levied by the supplier in the state of origin.
4. A general exemption from the described system is foreseen to avoid the levy of the tax in the state of origin. When the customer has a status of "certified taxable person", the supplier will not charge the VAT due to him. The customer is supposed to self-assess the VAT in his country, i.e. destination country as is currently the case. "Certified taxable person" means an enterprise globally considered by its tax administration to be a reliable taxpayer, which is the holder of a corresponding attestation (European Commission, 2017: 8–9). This system is undoubtly more advantageous for both parties of the transaction, but represents a parallel way deviating from the main method of levying the tax by the supplier.

2.4 Rates

The VAT rates have never been unified between member countries. Nevertheless, in order to prevent the distortion of the EU single market, the VAT directives in the early nineteens determined at least minimum rates – standard and reduced.

The Commission thought that a too low rate could distort the flows of goods between member countries, especially if the VAT is charged in the origin country. Lower VAT rate would mean lower price of goods

and consequently an advantage for producers of that country to the detriment of producers in other countries. Even if the VAT was in fact charged in the destination country as a provisional solution, for the sake of precaution the VAT directive contained also an exhaustive list of products and services where the reduced rate could be applied.

This rigid system was not avidly admitted by many member states. A convincing example is the reduced rate for restaurant and catering services, not included in the reduced rates list. In 2006 almost a half of member states enjoyed an exemption, and some of new East-Europe members would welcome the reduced rate as well.

We must point out, that the rigidity of the reduced rates system has led to a big number of individual exemptions claimed by the majority member states. There were (and still are) four main categories of exemptions (apart from very special cases):

- Temporary exemptions granted to new member states.
- Other individual exemptions granted by the Sixth VAT Directive 2006/112/EC on the common system of value added tax.
- Member States which, at 1 January 1991, were granting exemptions with deductibility of the VAT paid at the preceding stage or applying reduced rates lower than the minimum laid down in Article 99 may continue to grant those exemptions or apply those reduced rates (Art. 110 of the Directive).
- Particular cases, e.g. member states may apply a reduced rate to the supply of natural gas, of electricity or of district heating, provided that no risk of distortion of competition thereby arises (Art. 102 of the Directive).

In 2009 the first wave of the liberalisation of VAT reduced rate comes with the Directive 2009/47/EC amending Directive 2006/112/EC as regards reduced rates of value added tax. The Commission apparently came to the conclusion that a wider assertion of the reduced rate will not be dangerous for the functioning of the internal market and will, on the contrary, correspond to the legitimate needs of member states.

A true revolution is coming now with the general VAT reform. Whereas the Commission abandoned the VAT taxation in the country of origin once

for all, it could make without any risk additional unprecedented concessions in allowing the reduced rate in much more cases. The portion of the VAT reform concerning the reduced rates allows member states to use

- two separate reduced rates of between 5 % and the standard rate applied by the Member State;
- one exemption from VAT (or ‚zero rate‘);
- one reduced rate set at between 0 % and the reduced rates.

In total, each member state may apply up to four reduced rates (one of them may be a total exemption of VAT).

In addition of that, the current compulsory list of items permitting the application of reduced rate will be abolished. A new list will be established following the opposite concept. It will contain products to which the standard rate must be applied (e.g. alcoholic beverages, tobacco, gambling).

In connexion with the liberalisation of reduced rates all exemptions mentioned above will be abolished as redundant.

3 Conclusions

It is not possible to assess the introduced VAT reform for intra-Union transactions in this moment. It is very complex and we must certainly expect possible problems not apparent at the present stage. Nevertheless, the comparison of the new concept with the current state may tell us a lot.

1. The new concept is truly realistic. The principle of country of origin was finally abandoned in favour of the destination country. There are at least two enormous advantages of this change:
   - We may hope that the VAT fraud will be considerably reduced, since the goods will not be leaving the state of origin untaxed.
   - The principle of the destination state made possible a liberalisation of VAT rates.
2. The reform has brought much more flexibility to the system of VAT rates in member states. Their rigidity, typical for its early stage (France in the fifties, permitting only two rates) has been forgotten. The VAT in the Union scale ceased to be simple and universal (Bartes, 2018: 9).

Nevertheless, it fits much more to the needs of member states. More than 200 individual exemptions will be replaced by a very flexible system of multiple rates making the exemptions redundant.

3. Potential problems:
   - Application of foreign rates by the supplier might not be easy. As an aid for suppliers accounting for the VAT, a One Stop Shop will be introduced in each member state for them.
   - The existence of two different parallel regimes may complicate the functioning the new system – apart from the new one (levy of the VAT in the state of origin) the actual procedure will remain possible in parallel for certified taxable persons in the destination state.

4 General conclusion

It is obvious that the reform as a whole meets the needs and interests of member states. Some partial problems will certainly be overcomed. The assumption presented in the introduction has been confirmed.

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TAX LAW – SELECTED PROBLEMS

Tax Law versus Business Environment[1]

Vladimír Babčák[2]

Abstract

In his paper, the author deals with some theoretical and practical issues of influencing the business environment in Slovakia by the standards of tax law. Regarding the limited scope of the paper, he mainly focuses his interest in the field of direct taxation. Attention here is of specifically focused on the possibilities of tax law in improving the business environment and promoting the economic growth, strengthening entrepreneurship, transparency, and the application of fiscal justice in taxation, by also emphasizing the need to encourage taxpayers to comply with tax discipline.

Keywords: Tax Law; Stability of Tax Law; Improving Legal Certainty of Entrepreneurs; Tax Incentives; Transparency; Tax Fairness.

JEL Classification: K34; O44.

1 Introduction in the Set of Issues

McGee (1997) noticed that any impact of tax law may have a social dimension. After the year 1989, and especially in respect of the so-called first tax reform of 1992, Slovakia witnesses a significant increase in public interest in taxation and tax matters in a wide array of material and procedural contexts. The tax issues have begun to be a matter of serious concern by not just the professional community but also by the taxpayers themselves. This was mainly related to the fact that the change in the social and political system

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in Slovakia meant also transferring part of the responsibility in the tax area from the State authorities and employers to specific taxable entities. Both natural persons and the emerging business sector entities (irrespective of the legal status of individual entrepreneurs) have begun to be subject to tax-law regulations which presumed and in fact required much greater accountability to the State (however, this also relates to the relationship with the areal self-government) in the area of tax return and its subsequent settlement and fulfilment of a number of both directly and indirectly related different monetary and non-monetary obligations.

Slovakia (including some other post-communist countries) has begun to take over instruments and institutes of tax law in effect in foreign countries, especially those that are generally considered to be economically developed and are also characterized by the long-term application of democratic standards of governance. Despite the differences in historical, economic, social, demographic, different traditions and customs, etc. the post-communist countries have been "motivated" to approximate their tax systems to the economically advanced countries of Europe, especially to gradually eliminate the differences among them. After the accession of Slovakia to the European Union in May 2004, these differences began to mitigate even more. Although such a statement may refer to the area of taxation and several aspects of taxation, but it is not so clear a case if we are to talk about the support of the business sector through positive incentives for tax legislation standards.

The status and significance of tax law in Slovakia is affected by the overall social, political, and economic reality. Tax-law standards affect tax relations by way of regulation and repression primarily to ensure the fiscal interests of the State and, subsequently, the municipalities. Fiscal interests are, in our opinion, even though not so much emphasized by official policy, underpinned by the State's most overwhelming public interest; but we are not far from the truth that this is in operation in at least most of the modern states, if not all of them. At least rom this point of view one is entitled to say that taxes and their legislation are a significant factor in influencing the economy and affecting the legal status and development of individual entrepreneurs who in relation to the State budget are also parties to tax and legal relations. The resulting tax liability of taxable entities actually influences life in Slovakia

and satisfies the needs and interests of its inhabitants. That is why, in this sense, the tax-law issue is a grateful subject which is welcomed by politicians, economists, and lawyers, as well as by representatives of various other professions, such as psychologists, sociologists, and others.

Tax law, as a part of public law, has direct links to the economy of this State (both in its national and international contexts) and its taxable entities. In this idea, the focus of this article is also "hidden", the aim of which is to approximate the relationship between tax-law regulation and the business environment in Slovakia, more boldly expressed as influencing the business environment through tax-law standards. In this context, we wish to emphasize that the State interferes in the business sector with its whole arsenal of tax instrumentation, with its frequent interventions are pretty often little justified or incomprehensible. In any case, however, it may be noted with calm conscience that for each of these interventions it is necessary to see the fulfilment of the fiscal treasury of the State, i.e. the State budget.

The underlying argument from which our article is based om is that economic growth in Slovakia is not possible without the support of the business environment that will be competitive, relatively stable, unburdened by excessive bureaucracy, and unbridled by unreasonable legal regulations. Within the meaning of this thesis, support for entrepreneurship in Slovakia is dependent on several factors:

- on the competitiveness of the different segments of the market, each other and within a given segment;
- on the relative stability of the business;
- on the minimum bureaucratic burden of tax administration for taxpayers, including the low administrative burden on business;
- on eliminating the undesirable/inappropriate legal regulations.

In relation to the above thesis, two questions arise: (1) whether the present situation in Slovakia may be evaluated accordingly and (2) what is the share of tax-law standards in this situation?

2 Influencing the Business Environment by the Standards of Tax Law

Tax-law standards act on the sphere of social relations they regulate, directly and immediately, without any conditions on the part of other branches of law. Thus, tax law is not directly dependent on other branches of law, and thus freely and independently constructs its own legal institutes. However, this does not mean that the tax-law standards operate in practice in isolation. If that were the case, there would be nothing else but to admit that tax law is independent of other sectors, notably public law, but it does not yet guarantee its smooth application in tax practice. In order for tax-law standards to work more efficiently/effectively to develop the business environment, they must comply with the legal standards of other branches of law, paradoxically above all in the sphere of private law (first of all the commercial law). In legal practice, the relationship between industries that originate from two historically distributed and traditionally accountable groups of law – public and private, is thus shaped. However, this is only an abstract and theoretical view, since their symbiotic action in the area of business of tax subjects will be decisive.

The focus of tax policy support for the business environment should be guaranteed in particular by the rules governing direct taxes, as well as the area of indirect taxation. However, it cannot be overlooked that other legal regulations that we do not consider as genuine sources of tax law also allow the promotion of the business environment in the field of taxation. This will concern legislation that governs, for example, State aid, investment aid, R & D incentives, etc. We believe that it would not be entirely right in this context to make a dividing line between the original tax legislation and the related legislation.

There are likely to be only a few opponents who will not agree that tax law may be activated in a positive or negative manner in relation to the business environment. It also depends on whether it participates in the promotion of economic growth.

Taxes, their amount, method of payment, tax advantage or disadvantage of various business activities, etc. also affects the decision-making

of business entities on their economic activity. As a result, tax-law standards have the ability to create favourable economic environments for the development of commerce and business, but on the other hand, this atmosphere can even negatively affect and actually dampen such an air. In fact, this is also pointed out by the representatives of Slovak science on business or economic law (Suchoža, Husár et.al., 2009: 71; Suchoža et.al., 1998: 50; Husár, 2007: 25). Favourable business climate should allow undisturbed development of business activities and at the same time should not become an obstacle to such a development.

The primary factors that have a positive or negative impact on the business environment should also include the extent and framework of the prevailing principle of taxation. As diametrically different and contradictory in this respect, for example, the relationship between tax efficiency and tax fairness is perceived.

The relationship between the principles of tax fairness and effectiveness of taxation and their specific application at a given time is a clear indication of a link between politics, economics, and tax law. The Slovak tax law is being overridden by political influences and interests more than other branches of law. The real needs of this country's economy, created and developed primarily by business companies and individuals (as entrepreneurs or as employees), are often secondary to tax law. The policy is projected into tax-law regulation and this affects the economy, i.e. companies and other entities involved in the economic growth, and this is reflected back in the approach of political parties and taxation movements to individual entities of economic activity. Therefore, as one of the principles of the construction of Slovak tax law, a political compromise is recognized as a result of legal regulation, which is conditioned by the necessity of materially securing the activity of the State and the local self-government (Babčák, 2010: 44).

The current Slovak tax and related legislation enshrines a number of institutes and tools designed to help support the business environment. It is an instrumentation that cannot be denied a systemic character, although it is true that some of them could not go through a more critical and objective assessment of systemic requirements. For example, a valid law on income

tax (Act on Income Tax, as amended), in view of the existence of several dozens of tax exemptions and non-tax revenue cases, may be considered as a non-systemic instrument of the State, except that we consider all cases of exemption and relief as a systemic element transformed into a non-systemic law.

Analysing the past ten years in Slovakia, it may be concluded that in that period, some non-systemic instruments were also present in the area of corporate taxation, alongside with the instruments of systemic nature. Let us say at least two examples, which at the time "stirred up" the silent waters of the business environment. One concerned the establishment of an institute called the "tax security", which applied to the so-called risk persons who, in connection with the VAT registration, were forced to lodge a security for this tax and the second one pertained to the establishment of the "Tax Licensing of Legal Entities" institute. Both of these non-systemic measures reveal the primary fiscal interest of the state in obtaining funds for the State budget. Both of these cases, although one relates to the VAT and the other to the income tax, are similar, because what is associated with them is the application of Article 273 of Directive 2006/112/EC on the Common System of VAT (Council Directive on the Common System of Value Added Tax).

The tax security was introduced in 2012 by the VAT institute and cancelled on 1 January 2019. The security had to be deposited either by a cash deposit to the revenue authority bank account or by a bank guarantee provided by the bank without reservation. The amount of the security, which was deposited for a period of 12 months, ranged from EUR 1 000 to EUR 500 000, depending on the revenue authority's assessment of the potential risk of abuse by the registrant's VAT system.

According to the explanatory memorandum to the amendment to the Value Added Tax Law Act (Explanatory note to Law Act No. 369/2018 Coll., Amending Law Act No. 222/2004 Coll. on Value Added Tax, as amended: 2) that institute was abolished on 1 January 2019 because "*It appears that the tax security as an institute introduced in the VAT Law Act 2012 in order to eliminate the negative consequences of VAT arrears caused by newly-registered tax payers, is no longer needed to effectively combat tax fraud. It is therefore proposed*

that this institute be abolished". In view of the problems that VAT tax frauds are currently causing, such a justification by the Ministry of Finance of the SR as a draft amendment to the law act is at least absurd. We do not want to call into question the abandonment of this institute, just the contrary, we believe it should not have been set aside because it has merely complicated the already difficult conditions for doing business in Slovakia. Moreover, it did not increase the credibility of the so much proclaimed principle of legal certainty for entrepreneurs in the area of taxation, rather on the contrary, it supported legal uncertainty at least on the part of taxable entities. The formulation at the time of the law in force that the tax administrator, when deciding to impose a tax security, "*shall take account of the risk of VAT arrears*" is anything but a clear explanation of the reason for which it will determine the amount of the security at such a rate and not a different amount. In addition, the obligation to lodge the security originally applied to entities which, at the time of filing the tax registration application, did not carry out the supply of goods or services, but only carried out preparatory activities for doing business, so it was difficult to consider, in relation to it, any risk persons. We would also like to add that the explanatory memorandum to the amendment to the VAT Law Act 2012 (Explanatory note to Law Act No. 246/2012 Coll., Amending Law Act No. 222/2004 Coll. on Value Added Tax, as amended:14), referring to the introduction of this institute, 273 of Directive 2006/112/EC, which only allowed Member States to impose other duties necessary for the correct collection of VAT and the prevention of tax fraud. The text of this article states that: "*Member States may impose other obligations which they deem necessary for the proper collection of VAT and the prevention of tax evasion provided that they meet the requirement of equal treatment for transactions carried out in the national and transactions effected between the Member States by taxable persons and provided that such obligations do not result in border clearance formalities in trade between Member States*".

It would be interesting to have information on the number of taxable entities and the amount of the security that was collected by the financial administration at the time of its application (between 2013 and 2018). In that regard, the principle of legal certainty is also undermined by the fact that the applicant for VAT registration was not entitled to adequate interest

on the assets forming the security, even if, after the expiry of the twelve calendar months, the security had been repaid in full (in simplified terms, that it turned out that in this case it is not a so-called risk entity). It is all the more bewildering that the revenue authority has "profited" for a period of time from the funds providing a tax security, even though it was legally not a means at its own disposal[3].

The problem of the provision for the lodging of a tax security was also related to the fact that the criteria for determining the amount of the security were not transparent. It means that the law itself did not guarantee objectivity of the decision on the amount of the security, so it could happen that even a virtually bona fide person could have a certain security imposed close to the upper limit.

One of the principles that could have been affected by the introduction of a tax security institute is also the principle of proportionality. This requires that the action taken is appropriate to attain legitimate objectives (to attain the objective pursued by national law) and does not go beyond what is necessary to achieve those objectives, that is to say that such measures are to the least extent interfered with objectives and principles laid down by the relevant Union legislation. The EU Court of Justice has repeatedly pointed out the requirement formulated in this way (Court of Justice: joined Cases C-286/94, C-340/95, C-401/95 and C-47/96).

Regarding the tax license of a legal entity, it was applied in Slovakia from 1 January 2014[4] until 31 December 2016[5]. It had to be a sanctioning tool against indecent entrepreneurs, but it was only a tool for securing the above-standard tax revenues by which the then government wanted in essence only to demonstrate its "successful" taxation policy.

3 Absence of interest payments on compound tax assets can be compared to unpaid interest from excess depreciation which has been paid out and checked by non-spot checks. In such a case, the entrepeneur shall be entitled to interest for the period of 'extension' of the tax audit, as is also clear from the European case-law, such as Molenheide and Others C-286/94 (paragraph 63) and Enel C-107/10. Available at: https://m2b.sk/blog/pozor-na-povinnu-registraciu-k-dph-a-vysku-zabezpeky-je-vymahatelna-i-exekucne

4 It was introduced by Law Act No. 463/2013 Coll., Amending Law Act No. 595/2003 Coll. on Income Tax, as amended.

5 It was repealed by Law Act No. 341/2016 Coll., Amending Law Act No. 595/2003 Coll. on Income Tax, as amended; Act No. 580/2004 Coll. on Public Health Insurance and Law Act No. 95/2002 Coll. on conducting insurance, as amended.

The whole process of having introduced this institute was unusual primarily in the absence of a standard commentary on its implementation. In particular, in the explanatory memorandum to the draft law approved on 3 December 2013, there was no mention of the reasons for the introduction of the tax license, which in the case of such an important and doubt-making instrument should certainly not be lacking, then a draft law was tabled in January in which it was proposed to cancel the tax licenses. However, the draft law was only debated at first reading, and by Resolution No. 1021 of 5 February 2014, the Parliament decided not to continue the negotiations on this draft. Finally, the tax license was being applied for three years, which is too short a period to be perceived by the professional public as a tax instrument of a systemic nature. In essence, it was the so-called the "loss tax", with the amount of the license ranging from EUR 480 to EUR 2 880.

The amount of the tax license itself was almost liquidating for many small businesses. However, it did not even motivate large companies, given that they were withdrawing the financial resources they could use for their development programmes. Such an instrument penalized not only by indecent but also decent entrepreneurs. In addition, it has to be stated clearly that the tax license was strongly targeted against entrepreneurs who became voluntary VAT payers (as they did not achieve the statutory turnover for the VAT registration obligation in the VAT Act (Act on Value Added Tax, Art. 4/1)), which was also echoed in the Parliament's deliberations on the introduction of tax licenses. Such targeted reliance on voluntary registration as a VAT payer was linked to the fact that the taxpayer was subject to a double tax credit compared to a non-VAT payer (EUR 480/EUR 960). Unfortunately, the Tax Licensing institute did not take into account the fact that the entrepreneur's profitability is not guaranteed always and without exception. For example, larger expenditures on the recovery of tangible and intangible assets do not take effect after several years, which in practice may mean that the entrepreneur will report a tax loss. From this, it is not yet possible to conclude that such a taxpayer is a tax fraudster and should therefore be entitled to be paying double the amount of the license.

In view of the fact that the VAT is harmonized throughout the EU, only those obligations enshrined in this Directive and the subsequent legislative

acts and relevant national VAT laws implementing them are applicable to persons registered as taxable persons for VAT purposes. Obligations beyond the scope of the Directive may be imposed by Member States only if the Directive itself and the related acts allow it. This follows from the abovementioned Article 273 of the Directive. In this respect, reference should also be made to the judgment of the Court of Justice of the EU, which highlights the principles of proportionality and VAT neutrality. The judgment states that "*Moreover, the Court has already held that the measures which the Member States have the option of adopting under Article 273 of Directive 2006/112 in order to ensure the correct levying of tax and to prevent tax evasion must not go beyond what is necessary to achieve these objectives and must not be used in a way that questions the neutrality of the VAT.*" (EU Court of Justice: C-385/09).

We take the view that tax licencing exceeded the scope of interest of the VAT collection, taking into account that other instruments already exist to ensure correct VAT collection (for example, a summary statement, a check-report, etc.). It is not essential that the Tax Licensing institute was modified by the Income Tax Law Act and not by the VAT Law Act. Since, by way of example, the instrument in question has a non-pecuniary nature (unlike tax licenses), there is nothing else but to consider that a tax license as a pecuniary obligation was introduced primarily for fiscal reasons.

What requirements should the instruments of a tax character be in the interest of developing the business environment? We believe that these requirements can be theoretically divided into at least three groups; from a practical point of view, however, these groups are overlapping because the requirements of the individual groups cannot be implemented without the corresponding legal regulation:

- In the area of administration, the aim of the instruments of fiscal nature should also include the objective of simplifying taxation;
- In the field of law, the objective of the operation of instruments of a fiscal nature should also include the sense of stability of business, linked to legal certainty, transparency, and fairness of taxation;
- Positive influence on entrepreneurial activity, in particular by providing various benefits for compliance with tax discipline.

Simplifying the taxation of businesses entities requires, in particular, the removal of administrative burdens for tax entities. Among the tools that simplify (can simplify) business entity taxation, the following may be included, for example:

- *Simplifying the calculation of the income tax base*, which is particularly complicated in particular in relation to small and medium-sized enterprises/entrepreneurs. Under current legislation, there are more than 20 deductible and 15 imputable items, which complicates the business of these business entities, in particular due to the lack of personnel or financial capacities;
- *Increasing the limits for the deduction of tax losses*, especially for small and medium-sized enterprises. From 2014, the tax loss can be deducted for a maximum of four consecutive tax periods, whereas by the end of 2013, entrepreneurs could deduct the tax loss in the first year following the year in which the loss occurred and that loss (from the year of loss) could only be deducted for the next seven years. The situation in this respect is also complicated by the fact that the entrepreneur is obliged to apply the deduction of loss during these four years at an equal amount, i.e. up to a maximum of 1/4 per year. In this regard, it should be borne in mind that entrepreneurs often achieve positive economic results only after several years, but the cumulative loss from their several-year efforts can only be deducted to a small extent. To this end, it is to be added that most EU Member States have no time-limited possibility of deducting tax losses, there are also States in the EU that have no limits on the amount of the loss deducted;
- Possibility of *lump-sum producing of expenditure* in relation to natural persons – entrepreneurs. The Income Tax Law Act in this regard is based on the fact that the taxpayer applies the expenses in the fixed lump sum. The only obstacle to this is the status of value-added tax. The lump sum in which the taxpayer may claim the expenses is currently uniformly set at 60 % of the total business income and other self-employment. However, this option is limited to a ceiling of 20 000 € per year;
- *Revision of the issue of payment of income tax advances*/tax prepayments. The amount of advances (monthly/quarterly advance payments)

is linked to the amount of tax accrued for the previous taxation period. However, the positive economic results of the previous year do not yet guarantee the profitability of the entrepreneur in the next tax period, which may lead to the fact that paying higher tax advances, at a time when they are not profitable, may disrupt their cash flow;

- *The possibility of keeping tax records in a simplified way* in relation to natural persons – entrepreneurs (especially small tradesmen). In accordance with the Income Tax Law Act, this option is applicable to a taxpayer who earns income from business, from other self-employment, from renting or from the use of a work/artistic performance, while applying expenditure in a demonstrable manner. If these conditions are met, it is not the responsibility of the taxpayer to keep accounting under the Law Act on Accounting. By the end of 2013, this possibility was limited by the fulfilment of two additional conditions: (1) the taxpayer was self-employed and (2) in the immediately preceding tax period, the income (revenues) not exceeding 170 thousand €. At present, none of these conditions apply. In addition, this option was restricted to income from business or other self-employment;
- *The possibility of breaking down the tangible assets to individual separable components* of tangible assets, if the entry price of each individual separate component is higher than 1 700 €. This also involves the transfer of some types of tangible assets from higher to lower depreciation groups, but also the increase in the entry price of tangible assets from 996 to 1 700 € and intangible assets from 1 660 to 2 400 € (this is a measure that should improve cash flow of the companies due to a lower tax liability);
- *Unification of tax collection* and related payments, in particular the various so-called insurance contributions within a single place. At present, tax, customs, and insurance payments are provided not only by tax administrators but also by insurance companies (Social Insurance Agency and several health insurance companies). This is a problem that can also be described as an *organizational (partly sectoral) fragmentation in the collection of mandatory payments*. Despite the fact that the above-mentioned questions have already covered in the material entitled "Concept of Reform of the Tax and Customs Administration with a View to Simplifying the Collection of Taxes, Duties, and

Insurance Contributions" (May 2008)[6] and based on it a document on this area under the title "Strategy for the Development of Financial Administration for 2014–2020" has arisen[7]", implementation of this document in practice has failed. This problem also involves the existence of several types of mandatory payments under the so-called insurance levies and differences in the measurement bases between them, to which are added the differences between the so-called insurance deductions and determining the tax base for income tax. This fact disproportionately administratively affects business entities that are both taxable persons, customs agents or insurance premiums payers, as well as the competent authorities in charge of collecting such payments;

- *Supporting further electronic financial reporting*. This could help entrepreneurs in various "standard" actions regarding their awareness (for example, of the state of tax overpayments or arrears, especially due to several risks arising from the existence of arrears, the control of the amount of tax paid by type of tax, etc.).

Stability and legal certainty, transparency, and fairness of taxation are the principles on which the modern taxation system is to be built. Naturally, it depends primarily on the quality of tax and taxation legislation, but also on the capabilities and knowledge of financial management employees to apply and implement valid legal regulations in taxation practice.

If we are to talk about the **stability of taxation**, this must be guaranteed by tax law in its substantive and procedural expression in the long run. This requires (inter alia) compliance in particular with the following requirements:

- that tax and tax legislation is not subject to frequent amendments to tax law acts,
- that amendments to the applicable tax law acts provide a sufficient time-span to familiarize oneself with their content,
- that amendments to tax laws be made only on 1 January of the new calendar year,
- that tax and taxation legislation be simple, clear, transparent, and comprehensible.

6 Also known as the UNITAS programme or UNITAS II.
7 November 2013.

If we were to assess the current situation in the field of tax and tax legislation on the extent to which it meets the requirements, we will inevitably conclude that the tax law in Slovakia is most affected by the non-stability of the public sector. The instability of tax law in Slovakia is significant and unsustainable within a long-term prospect.[8]. A number of amendments and new tax law acts, not just at the beginning of the new taxation period, but often also within its course, have been causing uncertainty for many years in the business community. Frequently, taxpayers will not even be given sufficient lengthy legislative time to get acquainted with the legislator's intentions.

So much needed stability of tax law does not even contribute to the fact that almost every period of change of governmental power every four years is being prepared and implemented a smaller or larger taxation reform or the amendments under this magnificent label, which, in fact, do not actually bring about any reform. The concept of reform should reflect the correction of errors based on experience, knowledge, and realistic possibilities to improve the current situation in the area, but they often bring even lower quality than the standards they had before their introduction.

The instability of taxation law standards inevitably *undermines the authority* of taxation law, which has been formed in Slovakia in difficult times for many years. Frequent changes in taxation law do not favour the transparency of tax laws. In the Slovak taxation "portfolio", we could even witness a situation when a new law act passed by the Parliament and published in the Collection of Laws was abrogated by another law even before its entry into force.[9].

Unstable tax-law regulation significantly affects also the quality of implementation of taxation law and taxation-legal relations. Given the not-quite stable economic and political environment and the lack of consensus in this area, the taxation-law standards are just a reflection of this state of the art. Taxation laws are too complicated, unclear, and poorly understandable, so they often require tax advisors, which is not entirely acceptable and

8 We have drawn attention to the problem of frequent amendments to taxation rules in more detail earlier; since then, this problem has continued to rise, particularly in relation to income tax and VAT (Babčák, 2016: 8–34).

9 This pertained to Law Act No. 354/2011 Coll. on Financial Administration.

usable to small entrepreneurs/traders in particular (due to the poor financial situation of these people). The serious consequence of this situation in this area is the very low level of tax-legal consciousness of the Slovak society, which is also natural and understandable in some respects.

The accompanying negative phenomenon of the unstable tax environment in Slovakia is also the ***absence* of legal certainty** of entrepreneurs. It causes undesired legal consequences for the business environment in Slovakia, which are also associated, for example, with the transfer of the seat of Slovak companies to the so-called tax havens or ending business.

The number of Slovak business companies that have an owner in the so-called tax havens by the end of 2017 reached 4 796.[10] For comparison, by the end of 2015, it was 4 701 companies, and two years earlier (2013) it was 3 853 companies[11]. From this it resonates that in the period from 2013 to 2017, the number of companies from Slovakia, which have an owner in the so-called "tax-haven" has risen by about 943 companies. Also alarming is the trend in the decline of companies in Slovakia in recent years (perhaps with the exception of 2018), which shows the following overview.

Tax transparency in the EU is seen by the Commission (Communication from the Commission "On tax transparency in the fight against tax evasion and tax avoidance"; Commission Communication, "Anti-tax package: further steps towards effective taxation and greater tax transparency in the EU") as a key element in simplifying and streamlining tax systems. If the fight against aggressive tax planning and harmful tax regimes involving tax fraud, tax evasion, and avoidance of tax payments is to be successful and effective, greater mutual openness and awareness among tax authorities and better intergovernmental cooperation is to be achieved across the Union. Consequently, businesses will also have to bear greater responsibility for using transparent and fair tax procedures.

The requirement for tax transparency is also linked to the requirement for fairness of taxation. **Tax fairness** is perceived by the public very

10 Available at: https://ekonomika.sme.sk/c/20738771/pocet-slovenskych-firiem-s-vlastniko-v-danovom-raji-vlani-mierne-vzrastol.html

11 Http://www.bisnode.sk, alt. http://www.webnoviny.sk

sensitively, considering it as part of the phenomenon of justice.[12]. In this regard, it should be noted that the term tax fairness is a very ***uncertain and vague*** notion of tax law science. In addition, it also contains an element of ***flexibility***, which would be brought up to the surface mostly with the changes in the ideas about the economic direction of a company.

Few of the representatives of the professional community are absolutely clear about what tax fairness is, to whom or what it is to be compared and judged, what is not yet and what already is tax fairness and how and by what means this fairness is/should be secured. It should be emphasized that the very principle/idea of tax fairness does not address the problem of the fairness of tax collection, but the way in which taxes are imposed/levied.

In contrast to other principles that are inherent in an optimal/good/objective taxation system, the essence of tax fairness is primarily ethical-moral, which means that it does not in itself constitute a legal phenomenon. While tax law may reflect to the prevailing views of the professional public, how to express income/consumption taxation, and so on in the form of a tax rate so that at least in certain single signs it coincides with the views of the lay public as well. However, this does not yet reflect the satisfaction of the larger society that the method and level of taxation by arbitrary tax (most often as income tax, even less the VAT or some excise duty) is approaching the idea of how fair taxation should appear (Babčák, 2016: 8–34).

It is easy to manipulate the public by the phenomenon of tax fairness. However, it is all the more difficult in relation to entrepreneurs, especially in view of the experience they have in their day-to-day entrepreneurial reality. This applies to cases where foreign investors are advantaged as tax-payers compared to national entrepreneurs, as well as to the fact that small and medium-sized enterprises have incomparably more difficult conditions for doing business than large multinational companies, and so on. Such manifestations of unfairness (both presumed and legitimate) relate not only to their own taxation issues but also to the whole complex of relations

12 In turn, justice is very closely linked to the observance of law in society. This idea is documented by the thesis known from ancient Rome, that the meaning of law is in complete justice = Ratio in iure aequitas integra (Rebro, 1995: 250).

governed by law, including commercial law, criminal law, etc., which are directly or indirectly related to taxation.

In this context, it is possible to state that the law is increasingly influenced by the political and, in particular, economic interests of political parties and movements, various lobbyist groups, the business community, as well as populist statements by politicians who want to engage voters (Babčák, 2015: 355). The possibility of specifically fulfilling the idea of tax fairness in the taxation legislation is so many times dependent on the objectives of the tax policy of the State, but also on the intentions and willingness of the legislator to reflect what appears to the public as tax-fair. In this respect, the application of tax fairness in the business environment is rather a hypothetical question than a real fact. In addition, especially from the viewpoint of economists, everything that happens in the tax system is either fair or efficient (Schultzová, 2015: 21). However, it should be added here that the more the taxpayer perceives tax rules as unfair, the smaller his barriers to tax evasion are (Babčák, 2015: 55). From all this, the conclusion follows that the issue of tax fairness is, above all, an issue of the perception and feeling of a particular entrepreneur whether the tax, its amount and method of depositing, is fair or is not.

Even after several centuries since the issue of tax fairness began to take into account economic science[13] and the current world-recognized (in particular) economic authorities give their opinions on that[14], the phenomenon of tax fairness in the tax practice of entrepreneurs is not reflected in such a framework so that it does not raise doubts about its fulfilment. This concerns not just Slovakia, but also other EU Member States. Otherwise, the EU would not be paying attention to this issue, especially not in recent years (Commission Communication "A fair and efficient system of corporate tax in the European Union: Five key areas to be addressed").

13 Adam Smith has formulated four tax canons in the Treatise on the Fundamentals and Origin of Wealth of Nations (The Wealth of Nations), among which he cited tax fairness in the first place.

14 For example, the requirements for a "good" tax system, which were formulated by R. A. Musgrave, including an even distribution of tax burdens (each citizen should have a fair share), and the tax system should be designed to meet the demands of a fair distribution of tax burden (Musgrave, Musgravová, 1994: 200 et. seq.).

The idea of tax fairness in Slovakia often changes its "face" and it actually manifests itself in the form of tax unfairness. This is particularly strongly felt by small and medium-sized businesses, on which in fact the Slovak economy is standing[15]. This is in practice manifested in a number of ways, for example by granting tax concessions and other benefits to foreign investors, to the extent that Slovakia is referred to as a country with a privileged/preferential tax regime (Babčák, 2018: 15; Leservoisier, 1996: 9), and the like (Babčák, 2016: 8–34).

In times of globalization, with its, for example, free movement of people or capital within the EU, modern European countries cannot allow unilateral national measures of a legal nature to restrict or even prohibit entrepreneurs from changing their place of business or place of business in another Member State/third country. Therefore, they have to seek other options than to "keep" their tax residents from the circle of business entities in the territory of their home state. One of these options is also to provide various benefits to those entrepreneurs who adhere to tax discipline. Slovakia began to take action in this respect in the recent past as well, for example, by highlighting the pro-client tax policy in the media. This was being pursued in the above/mentioned UNITAS programme. In a nutshell, it is to be mean that financial administration regards tax subjects as their clients, although it is difficult to deny that the legislation of all the tax administrators' activities is built on a relationship of superiority to taxpayers.

However, the positive influence of business activity on tax law may be supported by the State's latest initiative known as the "Tax Reliability Index". This is an institute that found its legal expression in Section 53d of the Tax Code (Act on Tax Administration (Tax Code and on Amendments to Some Law Acts as amended by later regulations).

15 According to data on small and medium-sized enterprises for 2017 processed by the Slovak Business Agency, small and medium-sized enterprises in Slovakia make up for 99,9 % of the total number of business entities. In the corporate economy, jobs provide nearly three quarters of an active workforce. Up to 97 % of them are micro-enterprises employing less than 10 employees.
Available at: https://www.finreport.sk/ekonomika/financne-aktuality-13-2018/ or http://www.sbagency.sk/analyzy-slovenskeho-podnikatelskeho-prostredia#.XDIt4sHsZPZ

The Tax Reliability Index is a new Tax Administrator's measure introduced into taxation practice with effect from 1 January 2018. The establishment of this institute results from the implementation of the Anti-Fraud Action Plan 2017–2018 and aims at creating an objective, independent and legally applicable tax rating, which will in particular have a motivational and preventive character, including specific tax regimes (benefits) for reliable taxpayers.

The Tax Reliability Index should help improve tax collection and improve the business environment. Highly reliable taxpayers could benefit from some legitimate benefits compared to less reliable entities, which should encourage entities to behave responsibly in relation to financial management.

The web site of the Financial Administration of the SR[16] contains the criteria for assessing the tax reliability of individual areas (such as adherence to tax rules and fulfilment of statutory obligations, observance of the law on the use of the electronic registration treasury, submission of tax returns and other mandatory statements and tax forms, payment of taxes and customs debt in a timely manner and in full, etc.) as well as the specific benefits for such taxable entities (for example, compliance with the application for tax or tax arrears in instalments (if the statutory conditions are met), making the request to authorize the postponement of the payment of taxes or tax arrears (if the statutory conditions are met), issuance of a statement of the status of a personal account within 15 days, prioritization of other acts in order to secure payment of the tax arrears prior to the commencement of the tax distrainment procedure, preferential performance of the local survey in advance of tax control for the purpose of verifying entitlement to repayment of excess VAT deduction, determination of the start date of tax control of excess VAT deduction in agreement with the tax subject, etc.

The Financial Administration of the Slovak Republic will only announce the entitlement to benefits (to special tax regimes) to reliable taxable entities on the basis of meeting the criteria. If the taxpayer ceases to meet these criteria during the year, the Financial Administration shall notify him/her

16 Available at: https://www.financnasprava.sk/sk/podnikatelia/dane/index-danovej-spolahlivosti

of his/her loss of benefit within 30 days from the date of the change in his/her eligibility status to special tax schemes (benefits).

Let us hope that the tax reliability index will not just become a modern marketing move of the Slovak Financial Administration, which wants to limit the determination of Slovak entrepreneurs to move their headquarters abroad. Specific cases of tax-reliable entrepreneurs' applications that will be addressed by the financial administration in the near future may be farfetched in this respect.

3 By Way of Conclusion

Interests (because what else it is when we talk about the relationship between tax law and business entities?) are manifested above all in the form of political interests. *Politics itself is nothing but the promotion of interests.* This is true regardless of whether we talk about economic policy, social policy, etc. and within their frameworks about politics of taxes, fees, finances, and so on. Interests have their climax in assuming the power, and the political power is at the same time the economic power. Politics is, from our point of view, *the most concentrated expression of economic interests*. Therefore, it is more appropriate for the politics of interests to be associated with the economic aspects of interests. *Today's political interests often stand above law and justice.* Without exception, this applies in particular to the sectors of law directly linked to the economy and social relations.

Tax laws are intended to reflect/express unambiguously, clearly, and convincingly the interest of the society/State in collecting tax revenue in the relevant budget without burdening taxpayers in an excessive way, disproportionately and without adequate counter-measures from an economic point of view. In the light of the above, it is necessary to raise the question whether the tax laws take account of all or most of the facts to be beneficial in a democratic society not only for the tax recipient (the State/municipality) but also for the taxable entities. One of the contextual problems of Slovak tax law continues to be the *appropriateness of the tax burden*, that is, what should be the level of tax rates for individual taxes. This is related to looking for the question whether tax laws take into account the fact that

there are certain borders/limits of tax burden (tax appropriateness) in each society that the State should not cross. Otherwise, there is a real risk that there will be a situation where the taxpayer is not able to pay the tax without jeopardizing his sources of income or property (Kosikowski, 2014: 4–10). Some authors (Schultzova, 2015: 20) speak of the so-called sensitive tax threshold in this regard. This limit has its significance on the one hand, both in terms of the fulfilment of the State's interests and the interests of the tax entity; on the part of the taxpayer, the sensitive tax threshold gives rise to an interest in doing business or doing a dependent activity, or vice versa, it negates that interest (Babčák, 2018: 41).

When determining the level of the tax burden, the tax law standards should take into account (1) sufficiency of tax benefits for the State budget/local government budgets, (2) consistency of tax rates of direct and indirect taxes but also (3) competitiveness of the tax system in relation to foreign tax systems (Babčák, 2014: 9–26).

Regarding the future of the development of the business environment and the proportion of tax law in that development, we are of the opinion that the profound changes in the tax legislation concerning the support of entrepreneurs in the next years cannot be expected. Moving the tax burden from direct taxes to indirect taxes as a tendency of the past period is most likely at its end. Individual Member States are likely to seek partial adjustments to ensure economic growth and a higher tax revenue. This is a simple way for the Slovak public authorities to find ways to save on public spending. The tendency to increase public spending is indisputable, in addition for politicians and political parties it is also "advantageous", unfortunately, to the detriment of the population of this country and, last but not least, of the entrepreneurs themselves, who are able to make this tendency realistic by paying their taxes. The fact that public opinion is "massaged" by the public authorities through phrases about unprecedented macroeconomic results and the "successful story of Slovakia", while average real incomes are not even close to the minimum wage level in Western democracies, is in fact secondary in this regard.

In the recent period of time, two new types of mandatory payments have been introduced into this tax system: one tax and one special levy, the nature of which is one of being a tax.

In particular, it is a tax on insurance (Law Act on Insurance Tax and on Amendments to Certain Law Acts), whose introduction cannot be much objected against, since it can only "catches up" with what has been common in most of the Western countries for a long period of time.

As a new tax-levy tool, referred to as a special levy on commercial chains, it came into this "portfolio" as of 1 January 2019[17]. In fact, this deduction will in its resulting effect suit those commercial chains that are to be subjected to it; it will allow them to reflect the 2,5 % levy in the prices of goods and with a higher level of inflation that has for long been spoken in the media, one may anticipate a higher than a mere 2,5 % increase. There is no authority/entity in Slovakia that would be able to prove to the commercial chains that in such price movements as Slovakia realistically expects, the 2,5 % levy is not translated into price rises. The more public officials persuade the public that this will not happen, their statements are all the less credible and have the opposite effect.

A fundamental but possibly revolutionary change could happen if the EU were to "break" the determination of the Member States to refuse to implement the CCTB model[18] with the outcome of the implementation of the CCCTB[19].

What are currently the realistic possibilities for tax law to apply to the business environment? We believe that tax-law standards must create or form favourable conditions for business development. This is considered to be one of the fundamental objectives of tax legislation in this area. In our

17 This was published in Law Act No. 385/2018 Coll. on the Special Levy on Commercial Chains and on amendment to Law Act No. 595/2003 Coll. on Income Tax, as amended.

18 ***Common Corporate Tax Base*** (Spoločný základ dane z príjmov právnických osôb. This was published in Law Act No. 385/2018 Coll. on the Special Levy on Commercial Chains and on amendment to Law Act No. 595/2003 Coll. on Income Tax, as amended.

19 ***Common Consolidated Corporate Tax Base*** (Spoločný konsolidovaný základ dane z príjmov právnických osôb) (Draft Council Directive on a Common Consolidated Corporate Tax Base).
The CCCTB is a system of common rules for calculating the tax base for companies resident in the EU and third country companies located in the EU.

view, in order to achieve this goal, it is essential to pay special attention to the following measures:

- Ensuring greater stability of tax-law regulation.
- Simplifying and clarifying the taxation of business entities, including in the form of a broad, universal tax base.
- Clarifying the system of compulsory payments of business entities to public budgets.
- Unifying the system of levying taxes, insurance premiums, and customs duties.
- Removing any excessive bureaucracy linked to the administration of a specific tax, including the reduction of administrative costs for tax administration not just for tax administrators but also for business entities.
- Unifying the general and the tax accounting.
- Allowing for more modern depreciation methods for tangible and intangible assets, for example, in addition to the possibility of a straightforward and digressive depreciation, to consider introducing extraordinary depreciation based on monthly depreciation.
- Creating the conditions for a distinction to be made between the taxation of personal income and the income of employees as entrepreneurs or employees. It is necessary to agree with the opinion presented in the sources that there are indeed higher risks for entrepreneurial individuals in earning the income, which should be compensated by the corresponding taxation method. This leads us to believe that such a situation is not in line with the requirement of fairness in taxation (Bakeš, 2010: 13).

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Judiciary Law-Making and Tax Imposition in a Statutory Law System. A Polish Example

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Abstract

This contribution deals with the phenomenon of judiciary law-making in the field of imposing taxes and other public levies in the Polish legal system, which is a statutory law system. The main purpose of the publication is to confirm the hypothesis about the existence of such a phenomenon in Poland and its broad scope, as well as to demonstrate the lack of justification for such courts' actions. The dogmatic and theoretical method of research was used.

Keywords: Tax; Law; Imposition; Judiciary; Law-Making; Court; Poland; Polish; Statutory.

JEL Classification: K34.

1 Introduction

The creation of legal norms by courts, based on the mechanism of precedent, is a natural phenomenon for common law systems. This does not mean, however, that judicial law-making does not occur also in the statutory law systems. This fact is more and more often noticed and emphasized today; At the same time, the important role of the judiciary in improving the legal system – especially by making it fairer – is emphasized (Drywa, 2015: 47–55, Dąbek, 2010: 803)[2]. Sometimes, however, the law-making actions of the courts lead to effects that are difficult to accept, taking into account the conditions of admissibility of the law-making interpretation, formulated in the doctrine of the tax law. The purpose of this article is to draw attention to the disadvantageous phenomenon of courts creating

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2 The notion of judicial law-making, however, is the subject of quite many controversies (Grzybowski, 2009: 50).

legal norms in the field of public taxation, increasing the obligations of taxpayers in an unjustified manner. Worth to mention, this phenomenon can be observed in Poland, which is – a state of statutory law system, rooted in the traditions of legal positivism.

2 The scope of the concept of judicial law-making

Before the proper consideration, it should be precised what – for the purposes of this article – will be considered the law or the legal norm. In the theory of law there are different concepts of law and legal norms, and the choice of one of them remains largely a matter of adopting a specific convention. Often, the choice of a concept can be useful for specific purposes, and not for others. At the outset, two understandings of a legal norm should be distinguished.

First of all, the legal norm can be understood as the rule of behavior resulting from the act of law established by the state and usually secured by state coercion. This concept is positivistic. Secondly, the legal norm can also be understood as the rule of behavior resulting from other sources, but also secured by state coercion. The source of law in the second concept may not only be constituted by statutory law, but also by another law-making fact. Seemingly, this concept can be seen as excluded from the Polish legal system due to the closed constitutional catalog of sources of law, limiting them to the statutory sources only (Article 87 paragraph 1 of the Constitution[3]). In Polish doctrine, however, it is argued that the very fact that the constitutional catalog of sources of law concerns only the sources of statutory law, does not mean that other law-making facts are totally excluded (Malecki, 2003: 63). What is more, if there are sources of law other than written legal acts, it becomes natural that limiting the catalog of sources of law by a constituted act (as in the Polish constitution) cannot take effect outside the domain of statutory law. Since the foundation of a broad, non-formal concept of the sources of law is the possibility of law being created from various kinds of facts, the regulations of the statutory law cannot change it. Also observation of the practices of applying law in Poland proves that

3 Konstytucja Rzeczypospolitej Polskiej z 2 kwietnia 1997 r. (Dz. U. z 1997 r. nr. 78, poz. 483 ze zm.) – Constitution of the Republic of Poland of 2 April 1997.

even in the statutory legal system there are actually sources of law other than written legal acts (the simplest and unchallenged example are non-statutory justifications in criminal law) – denial would be in fact exorcizing the past. Therefore, I must reject the positivist concept of law and the legal norm as it being too formalist. In its light it would be clear that a judicial decision could not be regarded as law in a statutory law system. This concept, anyway, does not explain exhaustively the phenomenon of a legal norm, for the behavior of individuals is in fact regulated not only by the wording of normative acts, but also – to a greater or lesser extent – by the application of law made by public authorities, including courts.

Naturally, not every decision of a court is a law-making fact. Judicial law-making can be understood very differently (Dąbek, 2010: 53). In this paper a relatively narrow approach will be used, since it best suits my main purpose – to show that courts in Poland often do create law in an unjustified way, entering too far into the competences of the legislative authority. A narrower approach to the concept of judicial law-making serves two purposes here: first, it limits doubts about the classification of given decisions as law-making, and secondly it helps to show that the law of a given ruling is an unjustified action in the light of universally recognized rules of interpretation, application and creation of law.

Scientific categorization of all existing law-making facts can be difficult, for it is difficult to reach any consensus as to what the law itself really is (Brożek, 2012: 287). In this connection, the notion of law-making is also explained differently (Grzybowski, 2009: 50). The starting point for determining the scope of this concept for the purposes of this publication will be the definition of law-making facts made by Z. Ziembiński, who indicated that the given action is law-making when it leads to a change in the scope of behaviors ordered or prohibited by law (Ziembiński, 1993: 50).

In relation to the foregoing, I will only talk about judicial law-making in relation to such cases, where the actual impact of judgments on social behavior – as well as the perception of rules so established as legal norms – is common. The strongest influence will therefore have the resolutions of the Supreme Administrative Court (SAC), which obliges each administrative court to comply with the interpretation given in the resolution. Similarly,

a settled line of interpretation (a series of judgments incorporating similar interpretation rule) will affect society – the more uniform, the stronger its impact will it have. Naturally, even a well-established line of interpretation can be broken. However, this is not a phenomenon frequent enough to offset the general view of the impact of established judicial lines on society[4]. As for single judgments, I will not consider them as law-making, because one cannot undoubtedly state that single rulings do make the society perceive a court's interpretation as a legal norm. An onefold judgment that goes beyond the positive law may be considered in later jurisprudence as simply violating the law. Therefore, it does not create a general and abstract norm – and thus it is hard in this case to speak about creating law at all.

To summarize the above, by judicial law-making I will understand situations where the impact of the ruling on social behavior is significant, causing social perception of the actions as being allowed or not allowed.

T. Grzybowski (Grzybowski, 2009: 57–58), also starting from Z. Ziembiński's approach, points out four basic types of law-making court decisions (ie, those that go beyond the linguistic boundaries of the interpretation)[5]:

- refusal to apply the generally applicable law due to the rule *lex falsa lex non est* – false law is not law at all (*contra legem* interpretation),
- concretisation of indeterminate phrases, e.g. general clauses, and formulating definitions regulating them (*secundum legem* interpretation),
- basing the decision on the analogy (iuris or legis) – as long as it is considered unacceptable in a given area of law (*praeter legem* interpretation),
- fulfillment of legal gaps (*praeter legem* interpretation).

The admissibility of the *secundum legem* interpretation regarding the interpretation of indeterminate terms in the law of public levies is not controversial. Undefined phrases with blurred boundaries of their meanings (such as "important reasons", "significant loss" etc.) give the authorities the right

4 As B. Brzeziński states, bitterly but accurately, *the concept of a "fixed line of interpretation" in Polish legal language means a situation in which judges are no longer willing to discuss the correctness of the adopted understanding of the regulation regardless of what intellectual values or axiology this understanding presents* (Brzeziński, 2013: 187–188).

5 He does so in the context of the NAC's resolutions; however, these conclusions can be extended to all court decisions, as long as they affect the behavior of individuals (especially due to the established lines of interpretation).

of a discretionary power within the law-applying decision. However, this is an interpretation within the wording of the act.

It is also relatively uncontroversial to use the *praeter legem* interpretation in favor of the taxpayer. I do not question the law-making nature of such judgments, but I do note that they usually find an appropriate axiological justification, often based on constitutionally protected values (in particular tax equality and legal security). The subject of this work is, however, the activities of the courts that do not find such justification. Its lack results primarily from the fact that the *contra legem* and *praeter legem* interpretation, applied to the disadvantage of the taxpayer, must be confronted with one of the supreme and oldest principles in every state that follows the rule of law: the principle of exclusivity of a parliamentary act in imposing public levies ("no taxation without representation"). In Poland, it is currently based on article 217 of the Constitution, according to which *the imposition of taxes, other public levies, determination of taxpayers, taxable events and tax rates, as well as the rules for granting tax reliefs and redemptions as well as the categories of entities exempt from taxes is provided by act of parliamentary law*, as well as article 84 paragraph 1 of the Constitution, according to which *everyone is obliged to bear burdens and public benefits, including taxes, specified in the act of parliamentary law*. The state cannot, therefore, demand payment of any public tribute if this obligation is not justified in the text of the parliamentary statute.

3 Limitations of law-making in the tax law

In the Polish doctrine of tax law, the prohibition of interpretation going beyond the literal meaning to the disadvantage of the taxpayer does not raise major doubts (Brzeziński, 2008: 93, 126, 133–135; Zieliński, 1998: 17–18; Morawski, 2006: 22, 78, 198; Maruchin, 2004: 20–21; Smoktunowicz, 1997: 11; Mastalski, 2009: 128–129). Tax law resembles criminal law in this respect. It is a branch of law that deeply interferes with one of the fundamental human rights – the constitutionally protected property right. Every legal element constituting tax obligation can therefore only result from the proper source of statutory law, and the imposition of public tribute can only be the result of statutory regulation. Interpretation that goes beyond the literal meaning of the words used in a statute (an acceptable range

of meanings used in the act) – for example by analogy – is possible only exceptionally and only in favor of the taxpayer. Since the basic way of transmission of normative content is the text of the act, the interpretation based on dictionary and grammatical principles, that is, linguistic interpretation, is of fundamental importance in the interpretation of tax law provisions. In principle, a taxpayer is not required to know non-linguistic rules of interpretation, so he should not be surprised by their result if it is unfavorable to him. Nor should he bear any responsibility for the errors of the legislator. A non-linguistic interpretation can therefore be applied to the detriment of the taxpayer only insofar as it serves the purpose of choosing among several possible linguistic meanings (i.e. resulting from a linguistic interpretation) of a given phrase. It cannot be applied to the detriment of the taxpayer when its result cannot be contained in the possible sense of language expressions contained in the statute. The principle of the prohibition of interpreting the taxpayer's interpretation to his disadvantage is also widely emphasized in case-law (Spyra, 2006: 85–87, Filipczyk, 2013: 236–239, cf. e.g. the judgment of the SAC of 2 March 2006, I FSK 736/05, judgment of the Supreme Court of 22 October 1992, III ARN 50/92, judgment of the SAC of 23 April 1998, I SA/Po 1782/97).

It is also worth noting that, according to the tax law doctrine, any interpretation that goes beyond the literal meaning is permissible only exceptionally, if the results of the linguistic interpretation are irrational and absurd, non-legitimate, harmful or violating constitutional values[6]. Then a court can withdraw from the that plain meaning. The linguistic meaning of the text, as the limit of interpretation, is therefore not an absolute limit – except that a strong axiological justification is necessary to cross this boundary, especially referring to constitutional values (judgment of the Constitutional Tribunal of 28 June 2000, K 95/99; Brzezinski, 2008: 65; Filipczyk, 2013: 88). If so, it should be considered whether it is possible to allow an interpretation breaking the literal meaning to the disadvantage of the taxpayer if there

6 I disregard here from the controversy over whether the general or administrative court is allowed to refuse to apply the provision of an act due to its incompatibility with the Constitution, or whether it can only file an appropriate question to the Constitutional Tribunal.

is a sufficiently strong justification[7], for example, an obvious absurd that can be easily seen by a standard addressees of the legal norm – such as the use of a given word in the plural instead of a single or an obvious punctuation mistake. It should be remembered, however, that the obligation to impose taxes and other public levies solely on the basis of a parliamentary statute is an extremely important constitutional value. So if one allows to break the "language border" to the detriment of the taxpayer at all, the justification for such breach would have to be heavier than the combined power of the constitutional principles of legal certainty and the "no taxation without representation" rule of article 217 of the Constitution (and even in this abstract perspective it can be seen that the possibilities to do so are more than limited). The court applying such an interpretation should, therefore, weigh all the conflicting values, and then – if stating that certain values outweigh the principle of the law's specificity and exclusivity of a parliamentary statute in imposing public levies – it should prepare a written justification of its ruling in detail[8]. Unfortunately, there are lines of rulings in Polish tax law jurisdiction that do not satisfy even this condition. I will try to show it below.

4 Law-making court decisions to the detriment of the taxpayer in Polish tax jurisdiction

4.1 Civil law partnership and local taxes

Under the provisions of the law of local taxes[9] taxpayers are natural persons, legal persons and organizational units, including unincorporated companies, being in particular owners, perpetual usufruct or owners of certain real

7 There is clearly such an exception in criminal law (Morawski, 2006: 81).

8 There are very few such judgments. One of them is the resolution of the Supreme Administrative Court of 22 June 2011 (I GPS 1/11), refusing to refund the excise tax overpayment in a situation when its economic burden was shifted to the contractor (this possibility does not arise from the statutory provisions at all). It is difficult to agree with the justification of this resolution (as evidenced by the number of dissents written to this resolution), although – contrary to the most of other judgments presented here – the court at least noticed that it was making a law-making interpretation and that this problem should be considered at all.

9 Real estate tax, tax on means of transport, agricultural tax and forest tax.

estate or means of transport[10]. The reference to the taxpayer's private law subjectivity is therefore indirect here – by indicating the object of taxation – but still it is clear: only private law entities can be taxpayers, since only they can be in the situation of the owner or possessor of property. Nevertheless, for a relatively long time in the jurisdiction of administrative courts there was a clear line of interpretation, according to which a civil law partnership could indeed be a property tax taxpayer (eg the judgment of the SAC of 25 April 2008, II FSK 226/07, the judgment of the SAC of 31 March 2005 r., FSK 567/04, judgment of the Voivodship Administrative Court (VAC) in Gliwice of 31 January 2008, I SA / Gl 167/07, judgment of the VAC in Kraków from 3 March 2009, I SA / Kr 1601/08, verdict of the VAC in Gdańsk on 19 January 2011, I SA / Gd 1014/10, judgment of the VAC in Warsaw of 9 September 2010. III SA / Wa 376/10, judgments of the VAC in Gliwice of 8 October 2014, I SA / Gl 472/14 and I SA / Gl 473/14, judgment of the VAC in Rzeszów of 16 July 2014, I SA / Rz 388/14, judgment of the VAC in Gliwice of 15 April 2013, I SA / Gl 206/13, judgment of the NAC of 4 December 2015, II FSK 2685/13). The courts were basing on a clearly defective reasoning, according to which, despite the fact that possession (or ownership) of so-called "partnership's assets" (actually, common assets of its partners) belongs to the partners, it is the partnership who is the taxpayer, because – due to the characteristics and legal nature of a civil partnership "*as a corporation, association, organizational unit of persons acting jointly […] to achieve specific partnership's objectives – this is a manifestation of the permissible autonomy of tax law*" (the judgment of the SAC of 25 April 2008, II FSK 229/07). Thus, the courts clearly admitted that the ownership of property to be taxed belonged to partners, and yet they imposed tax on the partnership.

Tax law indeed is potentially autonomous in relation to other branches of law, i.e. it can use its own conceptual or institutional apparatus, including giving legal subjectivity in the field of taxation to entities that do not have any subjectivity in the field of the private law (Karczyński, 2011: 98–105).

10 Art. 3 ust. 1 and art. 9 ust. 1 ustawy z dnia 12 stycznia 1991 r. o podatkach i opłatach lokalnych (tekst jedn. Dz. U. z 2018 r., poz. 1445), art. 3 ust. 1 ustawy z dnia 15 listopada 1984 r. o podatku rolnym (tekst jedn. Dz. U. z 2017 r., poz. 1892) and art. 2 ust. 1 ustawy z dnia 30 października 2002 r. o podatku leśnym (Dz. U. z 2017 r., poz. 1821).

However, it is up to the legislator to decide on whether to use this autonomy or not. It is not the task of courts to "autonomize" tax law in a situation where the legislator explicitly refers to private law institutions. It does not matter, therefore, that the ownership is carried out in connection to the organizational unit in the form of a civil partnership, as long as it is still the ownership of the partners. At the same time, there are no premises to build any analogies to partnerships other than the civil law partnership (i.e. the partnerships of commercial law), which do have private-law subjectivity. On the contrary, the goal of the legislator from the end of the 1990s (from depriving a civil company of the status of an entrepreneur) is to encourage the transformations of civil companies into commercial ones (Herbet, 2008: 111).

The standpoint of the courts was uniform until 2011, even though, since 2005, the doctrinal critique of this interpretation has intensified (Karczyński, 2012: 89), which ultimately led to the breaking of this line of judgments. Different rulings were issued by the VAC in Warsaw (judgment of 29 September 2011 file reference number III SA / Wa 270/11), VAC in Poznań (judgment of 19 November 2013, reference number III SA / Po 613/13), NAC (decision of 16 December 2014, reference number II FSK 2985/12, judgment of 29 January 2016, reference number II FSK 3264/13, judgment of 3 February 2016, file reference number II FSK 2368/14, from 20 October 2016, II FSK 1577/16, from 6 December 2016, II FSK 2014/16). The resolution of the SAC of 13 March 2017 (II FPS 5/16) put an end to the doubts, in which the court noted that *because a civil law partnership cannot be the real property owner or perpetual usufructuary of land under civil law regulations […], in the light of the provisions of art. 3 par. 1 u.p.o.l. it is not a taxpayer of a real estate tax. The tax obligation in this tax is jointly and severally liable to all partners in a civil partnership.*

This short quote makes in fact an exhaustive justification of the position adopted in the resolution of the SAC. It did not require any broader argumentation, given the explicitness of the statute's wording. The earlier case law neglected this clear meaning of the act. The justifications for these judgments referred to the argument about the alleged autonomy of tax law, but did not indicate any significant value (especially constitutionally protected

one), which would allow it to transcend the linguistic definition of the taxpayer of local taxes. This line was so uniform and long-lasting that it was possible to talk about the creation of a new quasi-legal norm, imposing a tax obligation on a civil partnership, disregarding the provisions of article 217 of the Constitution. The existence of this norm is evidenced by the fact that until recently these taxes were generally accounted for by partnerships, and not by their partners.

4.2 Employment of a taxpayer's spouse versus tax deductible costs

According to the article 23 para. 1 pt 10 u.p.d.o.f.[11] in the wording binding until the end of 2018, the value of the taxpayer's own work, as well as his spouse's or minor children's work were not considered as deductible. The purpose of this provision was undoubtedly to exclude from the tax costs the value of the own work of the taxpayer himself and of the family members cooperating with him, since this value corresponds in fact to income (Brzeziński, 2002: 449–450)[12].

The following quotation from the judgment of the VAC in Gorzów Wielkopolski from 9 February 2009 (I SA / Go 942/08) may be regarded as representative for the whole line of interpretation: "*The value of the work should be understood as all kinds of benefits paid […] in exchange for the work performed, as well as the amount of benefits received […] for the work performed by the spouse or minor children of the entrepreneur.*" Therefore, in the court's opinion, the term "value of own work" is the equivalent of the term "labor costs" and excludes both paid remuneration to the persons mentioned in the said provision, as well as all derivatives from this remuneration (judgment of the VAC in Gdańsk of 18 July 2017, I SA / Gd 565/17). That is also the standing of the VAC in Łódź in the judgment of 21 June 2016 (I SA / Łd 211/16) and the SAC in its judgment of 10 December 2015 (II FSK 2561/13) and 4 June 2013 (II FSK 1933/11).

11 Ustawa z dnia 26 lipca 1991 r. o podatku dochodowym od osób fizycznych (T. J. Dz.U. z 1509).

12 For example, if a freelancer, who does not have employees, included in his/her deductible expenses his/her time spent on work, using the hourly rate to determine the amount of that cost, he would never have actually obtained tax income.

Before this line was formed, the judgments were divergent: both unfavorable for taxpayers (NAC judgments: 8 October 1997, III SA 628/96, 21 November 1997, I SA / Kr 430/97, 10 November 1998 r., I SA / Ka 384/97, of 3 September 1999, I SA / Lu 537/98, of 7 February 2001, I SA / Gd 2349/98, judgment of the VAC in Bydgoszcz of 6 February 2006, I SA / Bd 667/05, the resolution of the SAC of 27 November 1998, FPS 15/98 was also important, which concerned a different, more detailed issue, but the SAC considered it obvious that the remuneration for the work of the taxpayer's spouse was also "value of work"), as well as – much less numerous – to the favor of the taxpayer. It is worth to mention the favorable NAC judgment of 21 August 1998 (I SA / Gd 1582/96) and 17 November 1999 (I SA / Gd 1855/98). In the latter, the court exhaustively and quite aptly explained that seeing "value of work" in a paid wage for work is not supported by any interpretative rule: neither language interpretation ("value of work" and "remuneration for work" are not the same notions – a wage is the price paid for the value of the work) or systemic (no use of the word "expense", usually included in the regulations excluding actual expenses incurred from tax costs, indication of "own work of the taxpayer", which by definition cannot be a subject to any remuneration), or teleological (the *ratio legis* of the discussed regulation is the exclusion from tax costs of the deductible time of the taxpayer and his family, which could be estimated in any way; there is however no justification to exclude factually incurred expenses for a family member's wage, which after all is taxed, too). The court expressed the assumption that a different view on the said provision is determined by the search for an analogy in the social insurance regulations regulating the principles of insurance for persons cooperating with persons conducting business activities (and excluding the possibility of paying social security contribution at employees' rates).

However, such analogy lacks a legal and also axiological basis. This can be proved by the internal contradictions and illogicality of such a position. In most judgments, the courts omit the argumentation concerning the said interpretation. However, the NAC stated in its judgment of 7 February 2001 (I SA / Gd 2349/98), basing on the arguments of the Constitutional Tribunal (taken from the judgment of 24 January 2001, SK 30/99) that the purpose

of this regulation is to make an employment of a spouse less profitable than of a third party, because of the possibility of deducting the fixed-rate costs from the income, as well as of the joint taxation of spouses. The legislator's objective was supposed to be the "*elimination of the possibility of deducting costs of income twice from a single source through the use of joint taxation of spouses*." However, first of all, the joint taxation of spouses is fully legal, with its intended purpose to lower the tax indeed (it mitigates the tax progression in the case of disproportions in spouses' income by averaging them before calculating the tax. Why should it be banned if one spouse employed another one? Secondly, the fixed-rate deductible costs can be deducted in any case of an employment (not only employment of a spouse), which – again – was decided by the legislator. The position of the court would have some axiological justification (but would it justify overriding the principle of Article 217 of the Constitution?) only in the cases where the employment of a spouse would be fictitious and its purpose would be only a tax advantage[13].

Of course, if the taxpayer were to use the fictitious employment of a spouse (or anyone else) in order to artificially lower the amount of tax, in such a case the deduction of tax deductible costs would be illegal. However, this model of tax fraud can be used in the same way with the use of family members as well as strangers, and above all, fraud should be proven and not assumed *a priori* in every possible case. In this light, it seems bizarre that the court (and the tribunal) said that the said provision does not violate the principle of equality before the law, "*it only makes it less profitable […] to make expenses for a work contract concluded with the spouse than with a third party.*"

Interestingly, the NAC stated in the judgment of 21 November 1997 (I SA / Kr 430/97) that the spouse's salary does not constitute a tax-deductible cost regardless of whether the incurred cost fully corresponds to the value of the work performed by him. Thus, the court clearly distinguishes the payment for work from the value of that work, and yet it states that payroll

13 Still other arguments against the position of the Constitutional Tribunal have been indicated by B. Brzeziński (Brzeziński, 2002: 447–448): firstly, the income determination concerns individual taxpayers, and the possible joint settlement is a separate action regarding the determination of the tax liability. Secondly, the provision concerning the exclusion of the spouse's work value from the costs had existed even before the spouses were allowed to settle jointly. Thirdly – for various reasons spouses may not have the right to settle jointly – which the Court did not consider at all.

expenses cannot be a deductible cost due to the article 23 para. 1 pt 10 u.p.d.o.f. And according to that act, only the value of work is excluded from costs, not its actually paid equivalent. Interestingly, the distinction between the value of a given benefit and the price paid for it is generally recognized by the courts (as well as the statute) in many other cases, for example in the area of partially paid services, transfer prices or the taxable basis for the sale of goods within the transfer tax (*podatek od czynności cywilnoprawnych*) provisions.

Unfavorable jurisdiction met with vast criticism of the doctrine. H. Litwińczuk (Litwińczuk, 1996: 9) assessed the said interpretation unfavorable for taxpayers, pointing out that in many other countries salary paid to family members is allowed to be included in the deductible expenses, provided that it is established on market terms and the work is not fictitious. Also B. Brzeziński stated that the discussed provision applies only to situations in which the work takes place without a clear contractual basis (and hence, without a specific remuneration), because in such cases it is impossible to determine the price for the work done and the amount of an expense to be deducted (Brzeziński, 1999: 297). Decisions unfavorable for taxpayers thus completely omit these teleological arguments, including the *ratio legis* presented at the outset.

The last favorable ruling in this case seems to be the judgment of the SAC of 4 August 2004 (I SA / Gd 460/01). Later, the unfavorable ruling line strengthened so much that when in 2018 the amendment to the discussed provision was planned (with effect from 1 January 2019), to explicitly indicate that the family member's remuneration is the tax-deductible cost, the government was proud to announce it would "allow" the deduction of spouse employment's expenses. This is the best evidence that the discussed court action was a law-making fact.

4.3 Burden of proof in tax proceedings

In the light of the provisions of the tax ordinance act[14], tax proceedings are proceedings of an inquisitorial (non-contradictional) nature. The only party

14 Ustawa z 29 sierpnia 1997 r. – Ordynacja podatkowa (T. J. Dz.U. z 2018 r., poz. 800 ze zm., hereinafter referred to as "o.p.").

to the proceedings is the taxpayer, whose matter is to be settled by the tax authority, who conducts the proceedings. The inquisitorial nature of these is evidenced by the content of articles 122 and 187 para. 1 o.p., which order that the tax authorities in the course of the proceedings should undertake all necessary actions in order to accurately explain the facts and settle the matter (this is called the principle of objective truth). Therefore, it is the tax authority's responsibility to collect and exhaustively examine all evidence. Only in some cases there are clear specific rules, shifting the burden of proof to the party to the proceedings (eg. art. 116 o.p., regarding the tax liability of the company's managing board members).

Nevertheless, it is commonly stated in the jurisprudence that the burden of proof in tax proceedings rests with the taxpayer, especially when it comes to proving circumstances favorable to him, for example deducting expenses in income taxes (see NAC rulings: of 22 February 2019, II FSK 602/17, 15 February 2019, II FSK 352/17, 22 November 2019, II FSK 3121/16, 9 October 2018, II FSK 699/18, 6 June 2018, II FSK 1516/16, 28 March 2018, II FSK 883/16). This claim is usually being justified by the fact that "*the construction of the provisions of substantive law turns the initiative in searching for evidence over to the party*" (aforementioned judgment of 9 October 2018; Stanik, 2007: 6, Hanusz, 2004: 54), as well as by the fact that "*despite the provision of art. 6 k.c. not binding in the tax proceedings, the logical rule resulting from this provision [that the burden of proof rests on who derives legal effects from a given circumstance – ŁK] is of universal nature (the basic evidence 'idea')*", and finally that *"the reduction of revenue for incurred costs is not an obligation, but the taxpayer's right to show that they were incurred in order to achieve revenues*" (inter alia the aforementioned judgment of 22 November 2018).

It should be emphasized, however, that tax proceedings, unlike civil proceedings, are not formally contradictory, i.e. it is not about agreeing with one of the parties, but about exhaustively recognizing the entirety of the circumstances of the case (Nowak, 2011: 137–138, 140–141; Dzwonkowski, 2013: 853; Brzeziński et al., 2004: 56–57). Therefore, it cannot be said that in tax proceedings, anyone derives legal effects from a given circumstance. The legal effects should be derived from the factual state of affairs, comprehensively recognized by the tax authority in accordance with the principle of objective truth.

There are also no correct arguments referring to the construction of the tax, which allegedly forced the transfer of the burden of proof to the taxpayer. To explain it on the example of income tax: the fact that the subject to taxation is income, and not revenue, is the principle resulting precisely from the very construction of this tax. Therefore, there is no reason to diversify the burden of proof regarding revenue from regarding expenses. The deduction of tax deductible expenses is therefore not a special exception, a special privilege of the taxpayer, but a rudimentary element of the tax structure – the same as any other. And therefore, the proof of the facts in this respect should not be differentiated due to the alleged dissimilarity of this element of the tax structure (Dzwonkowski, 2013: 858).

It is also important to distinguish the burden of proof as a legal norm from factual circumstances related to proving the evidence in tax proceedings (Brzeziński et al., 2004: 58; Dzwonkowski, 2013: 854, 856). It is obvious that the tax authority often not only does not have the evidence, but also does not even know where to look for it. In this respect, it is clear that the taxpayer, if he wants certain facts to be taken into account, should indicate to the tax authority evidence or facts allowing this evidence to be obtained (for example, indicate witnesses who should be heard). This is, however, a factual and not a legal circumstance – thus this is not about the burden of proof, but about the requirement of its presentation (Brzeziński et al., 2004: 58–59). If the taxpayer has already indicated circumstances indicating the evidence relevant to the case or submitted incomplete evidence, the tax authority should use this knowledge for a comprehensive search for further evidence, starting from calling the party to a wider explanation if their initial claims are too vague. However, in the practice of tax proceedings in Poland, tax authorities notoriously disregard this, justifying this with the burden of proof lying allegedly on the part of the taxpayer.

Eventually, it should be concluded that correct are only those judgments, which state, according to the literal wording of the provisions of the tax ordinance act, that "*in the tax proceedings the burden of proof, under article 122 in conjunction with article 187 § 1 o.p., is on the tax authorities*" (SAC judgment of 16 June 2005, FSK 2477/04) or that "*the obligation to carry out the whole proceeding as for the all factual circumstances, if nothing else arises from specific tax*

provisions, always falls on the tax authorities and cannot be passed on taxpayer" (SAC judgment of 20 March 1997, SA/Po 1459/96). In the current jurisdiction of the SAC – at least in terms of tax deductible costs (but also input VAT or all kinds of tax reliefs and exemptions) – this position is not respected, which means that the taxpayers invoking the provisions on the inquisitiveness of tax proceedings usually are ignored. This happens without a legal basis (Dzwonkowski, 2013: 855, 859), which is, in fact, even admitted by supporters of such activity, who indicate the "implied" imposition of the burden of proof on the party to the tax proceedings (Hanusz, 2004: 49).

4.4 Expenses for garments as tax deductible expenses

The specificity of many businesses requires appropriate attire of entrepreneurs or their representatives. When it comes to garments used typically for business purposes (for example: attorney toga, welder's suit, bus driver's uniform, bank employee's suit with a bank logo), in the light of the administrative courts' jurisdiction it means that it is not used privately (!) – consequently, there are no obstacles to include such expenses in the tax deductible costs[15]. It does not raise anybody's doubts that such an expenditure is used to generate revenue. Many entrepreneurs, however, purchase items of clothing, the nature of which does not limit their use only to business – for example, smart suits, elegant jackets, trousers, shirts, ties, shoes, accessories (watches, belts, scarves, hats), outerwear, etc. These elements in certain cases, however, may only be used for business purposes – and then there should also be no doubt that the expenses for their purchase should be considered as incurred in order to generate income, as long as in a given industry a particular type of outfit has a positive effect on the image of an entrepreneur (or his representatives). It should not matter then whether the outfit is specially labeled with an entrepreneur's logo or not. However, in the Polish jurisdiction, such expenses are a priori considered as excluded from tax deductible expenses. Courts indicate that they are personal in nature, that the aesthetic appearance is only about personal culture, and is not related

15 According to art. 22 para. 1 u.p.d.o.f. and art. 15 para. 1 of the Act of 15 February 1992 on Corporate Income Tax (Journal of Laws of 2018, item 1036, hereinafter "updop"), the tax deductible costs are costs incurred in order to achieve revenue or to maintain or secure a source of income (excluding some of the specific expenses indicated in the Act).

to business activity, or that obtaining income in a given industry is not dependent on the type of clothing worn, or that it is impossible to deduct any expenses which would be made anyway, even if the taxpayer did not conduct any business activity (eg. SAC judgments: of 2 March 2016, II FSK 3620/13, of 25 November 2015, II FSK 2213/13, of 17 October 2003, SA/Rz 2341/01, of 25 June 2003, I SA/Ka 1328/02, of 24 January 2001, SA/Sz 1875/99, of 15 September 1999, I SA/Wa 1261/98, 10 September 1999, I SA/Lu 742/98).

Interestingly, this position is completely inconsistent with the jurisdiction concerning other expenses. Let us take, for example, judgments allowing the deduction of expenditure on clothing associated with the company's image, eg. by affixing it with a logo or advertising inscriptions (judgment of the VAC in Warsaw of 31 July 2013, III SA / Wa 659/13, judgment of the VAC in Kielce of 2 September 2010, I SA/Ke 433/10, judgment of the VAC in Poznań of 28 February 2008, I SA/Po 1540/07). But how should a suit marked this way have a positive influence on the entrepreneur's revenue? Is a chairman of the board dressed in a suit with the company's logo and advertising slogans really going to enhance the company's image better than if he was dressed in a suit without these dubious decorations? In addition – if the aesthetic attire, as the courts claim, does not affect the revenues – why is it allowed to deduct expenses made for the aesthetics of an entrepreneur's premises? If it is obvious that, for instance, painting the shabby or dirty office walls positively affects the possibility of generating revenue, why the same criterion should not apply to the outfit of people representing the entrepreneur? Why the court does not state in relation to the expenditure for repairs, that "*it may have a positive impact in the reception of the represented company by contractors, but it is not required in the business,* and as a result *there is no direct cause and effect relationship […] between the expense and income gained by the taxpayer*" (the above-mentioned judgment of the VAC in Kielce of 2 September 2010 with a content representative for many other judgments, referred to also in this very ruling)? Why, in relation to spending on costumes, courts put – contrary to the *lege non distinguente* interpretation rule – the additional condition that a tax deductible expense must be "required" in the business? Why do they not set the same stipulation

to other costs, allowing to deduct, for example, expenses on computer equipment, a car or a mobile phone (actually, even if they are partly used for private purposes)? In most industries, there is no "requirement" to use this type of civilization benefits after all.

Naturally, in each case it should be considered whether the garment is actually used for business purposes and whether it does not constitute representation costs, explicitly excluded from the tax deductible costs. The very fact that a garment might not be used for business purposes cannot, however, lead a priori to exclusion of an expense from tax deductible costs. Nevertheless, for example in the abovementioned judgment of 25 November 2015, the SAC states that "*it is impossible […] to assume that the expenditure on a smart suit was incurred solely in order to obtain income from the applicant's business*", even though the dispute concerned an advance tax ruling issued for a case where the taxpayer clearly stated that the said suits will be used solely during business (tax advisory) activities. Thus, the court was not even formally entitled to assess this issue, since the advance tax rulings can be issued only within the boundaries of the facts described by the applicant. Ultimately, the court anyway concluded that *a smart suit, just like a shirt and other items of clothing, are by nature personal items, the purchase of which does not include in the tax deductible costs, regardless of whether and to what extent they are used in the course of the business.* However, the court did not indicate the legal basis for such a claim (not counting the general provision of article 22 para. 1 u.p.d.o.f.).

4.5 Transformation into a partnership and the tax on civil law transactions

The tax on civil law transactions is a tax on, inter alia, capitalization of companies and partnerships. According to article 1 para. 3 pt. 3 u.p.c.c.[16] a company's or partnership's transformation (change of its legal form) is subject to tax "*if it results in an increase in the assets of a partnership or an increase in the share capital of a company*". According to article 6 para. 1 pt. 8 letter f u.p.c.c. the tax base is then "*the value of contributions to a partnership formed as a result of the transformation or the value of the share capital of the company resulting from the transformation*".

16 Ustawa o podatku od czynności cywilnoprawnych z 9 września 2000 r. (T. J. Dz. U. z 2017 r. poz. 1150).

In the jurisdiction of administrative courts, a clear, completely uniform line of interpretation was developed, according to which the transformation of a company into a partnership or of a partnership into another partnership, that does not result in increasing its assets at the time of transformation, is subject to tax anyway (SAC judgments of 2 September 2015, II FSK 1797/13, 10 June 2016, II FSK 1313/14, 20 September 2016, II FSK 2452/14, 18 November 2016, II FSK 2846/14, 12 January 2017, II FSK 3745/14, 14 June 2017, II FSK 1477/15, 2 August 2017, II FSK 3697/14, 10 August 2017, II FSK 1724/15, 19 January 2018, II FSK 3640/15, 25 January 2018, II FSK 111/16, 1 February 2018, II FSK 242/16 – and numerous judgments of VACs). Most of the judgments concern the transformation of a company into a partnership, although recently similar (more controversial) rulings have appeared, regarding the transformation of a partnership into another partnership (judgment of the VAC in Poznań of 31 October 2017, I SA/Po 486/17, VAC in Kraków of 19 January 2018, I SA/Kr 1270/17, VAC in Wrocław of 5 July 2018, I SA/Wr 383/18).

According to these rulings, "increase in the assets of a partnership", referred to in article 1 para. 3 point 3 u.p.c.c., turns up when the partnership's assets at the moment of transformation are greater than the previous tax base (i.e. in almost every case of transformation into a partnership), because "*if […] considered […] that the transformation does not result in any asset gain on the side of a partnership, due to the acquisition of only the capital structure of a joint-stock company (share and reserve capital), then this claim could not be reconciled with the content of article 6 para. 1 pt. 8 letter f) u.p.c.c., which explicitly states that the taxable amount for the transformation of the company is the value of contributions to the partnership, as well as the regulation of art. 1 para. 3 point 3 u.p.c.c., which provides that the […] transformation of the company [is taxed – ed. ŁK], if its result is an increase in the assets of the partnership. These regulations would be in such case unnecessary, they would not contain any normative content, because there would be assets to be taxed. There would be no increase in the assets of a partnership as defined in article 1 para. 3 pt. 3 u.p.c.c., and it would be unnecessary for the legislator to establish in article 6 para. 1 point 8 letter f) u.p.c.c. a tax base for company or partnership transformations*" (the quote comes from the aforementioned SAC judgment of 1 February 2018 and is representative for many other judgments).

A detailed polemic with this standpoint would be too long for this paper (more: Karczyński, 2011: 191–194). It is enough to say that the courts apparently assume that it is not possible to make contributions to the company or partnership at the moment of transformation. Only with such an assumption could it be argued that the literally interpreted passages of the provisions of article 1 para. 3 pt. 3 u.p.c.c. and article 6 para. 1 point 8 letter f u.p.c.c. are unnecessary. However, the fact that most cases of transformations do not involve an increase in the assets of the company or partnership being transformed (because the contributions are not being made in the process), does not mean that it is utterly impossible to make contributions at the moment of transformation. Contributions may be made either by partners already participating in the company (partnership) or new partners joining the company at the time of transformation (Miś, 2005: 342–343). The fact that this solution is rarely used does not justify the claim that making contributions at the time of transformation is an empty term. If, however, no additional contributions are made at the time of transformation, then it cannot be said that any contributions to the company are being made during the transformation (Pinior, 2015: 1395, Szumański, 2009: 1133–1134; Miś, 2005: 351–352).

In the context of this paper's subject, the most important is that the courts completely ignore the explicit statement of the act that the transformation can be subject to tax only if it involves increasing the partnership's assets. What is perhaps the most bizarre, in many judgments it is pointed out that a solution other than applied by the courts would lead to a certain gap, a tax break in situations where the company being transformed would have created reserve capital either from accumulation of profits or from *agio* (surpluses of a contribution over nominal value of shares or stocks), which, as a result, would not be subject to tax. However, this (i.e. the existence of an alleged gap) is not true – indeed, the accumulated capital is not taxed, but the reason for this is not the literal interpretation negated by the courts, but the solution introduced by the legislator himself, freeing of tax the amount of *agio* and the reserve capital created from the accumulation of profit. After all, the reserve capital, created from *agio* or retained profit, in a company that is not subject to any transformations, is also tax-free. Why, then, would this capital be taxed at the time of transformation? The courts clearly appear here as the legislator, imposing a tax.

In conclusion, the claim on the need to tax the transformation of a company or partnership whose assets are not increased at the time of transformation constitutes a *contra legem* interpretation. The statute, as a condition of taxation of transformation into a partnership, indicates the increase in the assets of a partnership, which in most cases lost by taxpayers, did not occur at all. The jurisprudence line, due to its uniformity and universality, leads to the same effects as the change of law by an imposition of a new tax.

4.6 Social insurance contributions of sole shareholders

Law-making judgments appear also in the sphere of social insurance contributions. According to article 6 para. 1 point 5 of the act on the social insurance system[17], one of the titles to compulsory social insurance (and, consequently, the obligation to pay contributions for this insurance) is conducting "a non-agricultural business activity". Pursuant to article 8 para. 6 point 4 of this act, being a sole shareholder of a limited liability company is considered conducting non-agricultural business activity, too.

It would seem, therefore, that the partner of a limited liability company on the basis of the abovementioned regulation may reasonably assume that if he is not a sole shareholder, then his situation will not be treated as a compulsory insurance title. Unfortunately, this would be far from truth. In the judgment of 3 August 2011 (I UK 8/11), the Supreme Court stated that the person who concludes a contract of employment with the company in which he is the "almost sole" shareholder, from the perspective of the provisions on the social insurance system, cannot be treated as an employee, because in this case there is no element of subordination, appropriate for the employment relationship. An additional effect of negating the status of an employee (and paying social security contributions on this basis) is, in the light of this ruling, recognition as a title to insurance of being the "almost sole" shareholder of a limited liability company[18]. While one can agree with the negation of the employee's status (especially as in that case the employment contract was proven fictitious), it is difficult to find any

17 Ustawa z dnia 13 października 1998 r. o systemie ubezpieczeń społecznych (T. J. Dz.U. z 2019 r., poz. 300 ze zm.).

18 It may lead to the obligation to pay a higher or lower levy than the amount due from an employee – depending on the remuneration for his work.

argument that makes non-sole shareholder pay public levy for being the sole shareholder of a company – even if he can be called an "almost sole" shareholder. "Almost sole" is, however, not the same as "sole" – therefore, if the legislator himself sets a clear boundary here, the court should not move that border to the disadvantage of a taxpayer.

Nevertheless, this interpretation is commonly repeated in subsequent cases where a partner holds a stake of about 99 % in the share capital of the company – for example, the Supreme Court ruled so in verdicts: of 11 September 2013 (II UK 36/13), of 7 March 2018 (I UK 575/16) and of 13 March 2018 (I UK 27/17). The Court of Appeals in Szczecin suled the same in the judgments of 24 November 2015 (III AUa 129/15) and 19 July 2017 (III AUa 410/16). It should be noted that the new *quasi*-legal norm thus determined is a norm with very blurry borders, introducing a lot of uncertainty towards shareholders with slightly smaller but still significant share in the company's share capital. For example, in the judgment of the Supreme Court of 17 October 2017 (II UK 451/16), a 95 % share was deemed to enable the majority shareholder to act as an employee of his own company.

4.7 Return of overpaid excise duty, shifted to the buyer

Starting from 1 January 2006, Poland applied provisions on the determination of the taxpayer of excise tax on electricity non-compliant with the European Community law. According to the Polish law, the taxpayer was an energy producer (article 6 para. 5 of the act of 23 January 2004 on excise duty[19]), and according to EU regulations – the distributor (section 21(5) of Council Directive 2003/96/EC of 27 October 2003 restructuring the Community framework for the taxation of energy products and electricity, OJ L 283, 31 October 2003, page 51).

This meant that producers who had paid excise duty in violation of the abovementioned directive, could claim a refund of an unduly paid tax pursuant to art. 72 o.p. At the same time, the tax authorities could not rely on the directive in order to obtain a tax from the distributors – for the directive can be applied directly only in favor of the taxpayer.

19 Ustawa z 23 stycznia 2004 r. o podatku akcyzowym (Dz.U. z 2004 r. Nr 29, poz. 257 ze zm.).

In disputes of this kind, discrepancies initially appeared. Courts refusing to refund the overpayment referred to the civilian concept of unjust enrichment, but it was not based on tax law at all. Finally, on 13 July 2009, the SAC in a panel of 7 judges issued a resolution (I FPS 4/09), in which it recognized the possibility of refunding the overpayment in the above-mentioned situation. However, as early as on 22 June 2011, the NAC in the entire Chamber of Commerce issued another resolution (I GPS 1/11), changing the previous one. Comprehensively justifying its position, the NAC refused to refund the excess tax to excise taxpayers who transferred its economic burden to their contractors. To this resolution, as many as 8 out of 21 judges reported dissenting opinions, pointing its incorrectness.

A full reference to the NAC's arguments exceeds the scope of this paper (the abovementioned dissenting opinions would be a proper lecture though). However, the resolution in question is one of the few rulings of the SAC, in which the court refers at all to the arguments on the prohibition of law-making to the detriment of the taxpayer. This part of the ruling is worth referring to. The NAC emphasizes that "*the necessity to refer to the above interpretation directives (i.e. the primacy of the linguistic interpretation and the in dubio pro tributario principle) does not exist in relation to all provisions contained in the tax act, irrespective of the subject of such regulation. In other words, it is not the case that the mere fact that a provision is a provision of a tax act, requires the primacy of literal interpretation and the application of the in dubio pro tributario rule. The analyzed case does not directly concern tax burdens or public services. Constitutional axiology referring to the permissible directives within the interpretation of tax law is therefore not fully adequate to the discussed issue. Interpretative doubt in the present case boiled down to answering the question whether a taxpayer may exercise the right to refund an overpayment, if the inclusion of this claim would lead to his unjustified enrichment. Therefore, it is not a burden or a public service, not to mention a tax or other public levy. Recognition, as the Court has done in the present case, that a impoverished taxpayer has no claim for reimbursement of overpayment, does not lead to an increase or extension of any taxpayer's duty or to withdraw or limit his tax preferences.*"

Therefore, the NAC did not question the very prohibition of a law-making interpretation to the detriment of the taxpayer. His position, on the other hand, boils down to stating that the refund of overpayment of an unjustly

paid tax is not a tax issue, and the refusal of this refund does not limit the taxpayer's rights. It seems that further critical commentary is unnecessary.

5 Conclusion

The presented review of judgments is not exhaustive. Nevertheless, it seems to provide an adequate illustration of the phenomenon, present in Poland, of law-making to the detriment of taxpayer. It is apparently impossible to escape from the approaching of statutory to precedent law systems – it is a natural phenomenon in the modern globalized world (Drywa, 2015: 46, Kmieciak, 2006: 22, Martínez Pujalte, 2018: 164–165). Therefore, I am not opposed to the thesis about the very possibility of judiciary law-making. However, such actions should be justified in a way that refers to adequately significant values, especially constitutionally protected ones, such as, first of all, tax justice (Małecki, 2003: 69–71, Gomułowicz, 2008: 131–136). Therefore, it is difficult to accept law-making rulings unfavorable for the taxpayer, violating the constitutional principle of the exclusivity of the parliamentary statute in shaping tax liabilities – especially that the courts issuing such judgments usually do not sufficiently justify them. Indeed, the court creating a new legal norm should take responsibility for its proper justification, proving the validity of its decision in *jus* understood as unwritten rules of equity (Dąbek, 2010: 444–449, Gawarecki, 2015: 59–62). Imposing a tax by a court verdict, however, would need to be justified by a value stronger than the combined power of the constitutional principles of legal certainty and the "no taxation without representation" rule – which is hardly possible. Unfortunately, the courts too often do not pay due attention to this.

This phenomenon deserves a negative assessment, especially since such judgments, passed at the highest levels of the hierarchy of courts (in particular in the Supreme Administrative Court), cannot, in principle, be repealed (Brzeziński, 2011: 327, 329). This justifies the conclusion that the courts in Poland are interfering too far into the powers reserved for the legislative authority. In the field of taxation, the reservation is all the more important because taxes should only be imposed by bodies with appropriate legitimacy, obtained in general elections. Courts do not belong to such bodies.

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Tax Levied on Certain Financial Institutions and its Impact to the Polish Banking Sector and Polish National Budget

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Abstract

The aim of this paper is to presented the main challenges for the banking sector in the context of the Bank Tax Act, on tax from certain financial institutions. The main objective is to decide whether this tax will remain neutral for banking sector customers. For the purposes of this article, the authors hypothesize that this tax is not neutral. The authors want to show how the passing of the Bank Tax Act, affected the banking sector. The article consists of two parts. The first part of this article presents the essence of the tax on certain financial institutions and its effects on the financial sector. This section presents the legislator's arguments about the reasons for the introduction of the tax, as well as an attempt to compare with other similar regulations within the EU. The second part of this article shows the structure of the tax from certain financial institutions; entity, subject, tax base, exemptions. On this basis, some conclusions can be drawn as to the lack of consistency of the Polish legislator in the construction of the provisions of the Bank Tax Act. In particular, there are no protection provisions for customers/consumers who ultimately bear the burden of tax on certain financial institutions.

Keywords: Banking Sector; Taxation; Banking Law; Bank Tax; Tax Rate; Stability of Financial Market.

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1 Introduction

To analyze a new tax, imposed primarily on the banking sector, it is best to combined several values; the assumed by the legislature, level of revenue to the state budget from this tax and actual inflows and financial results of banks before and after its introduction.

It should be noted that this tax has a huge impact on the situation and stability of the banking system, what in consequence has a huge influence on the situation of the entire economy. We must also remember the fundamental rule that the bank competition rises the instability. (Kanas, Hassan Al-Timimi, Albaity, Mallek, 2019: 570) Since the introduction of the Act of 15 January 2016 it has passed more than three years. The time that has passed, gives the opportunity to make some, preliminary assessment. Unfortunately, due to the entry into force of the Act on 1 February 2016, the analysis will not cover the entire year. The first full fiscal year in which the new tax was in force was in 2017. Therefore, some simplifications are necessary and future conclusions may, or maybe even should, be corrected. Analysis for the purposes of this text, has used statistical analysis as well as the legal-comparative, descriptive and synthetic method. Futhermore, individual interpretations of the Ministry of Finance allowed the use of empirical analysis of specific cases.

The question also arises whether the new tax remains neutral to the public and whether only the banking sector bears its consequences. In fact, this tax is not neutral as it was announced by the Government. Even without a thorough analysis, it can be argued that this tax may ultimately be passed on to the sector's customers. The evidences of lack of this neutrality are provided in this article in further sections. In this case, the role of the legislature should be to take steps that will protect clients from the negative consequences of additional taxation of the financial sector institutions.

2 The essence of a tax levied on certain financial institutions, and its consequences for the financial sector

Article 4 of the Act on Taxation of Certain Financial Institutions, of 15 January 2016 (hereinafter, the Act), enumerates entities covered with this tax obligation, which shows, contrary to the popular belief, that the new tax is levied not only on banks but on other financial institutions, too. Thus, in the light of the Act, using the term 'a bank tax' appears to be a gross simplification. On the other hand, as much as 83,5 % of the revenue from this tax is contributed by banks, which seems to justify this colloquial name.[3] The subject scope and construction of this tax will be discussed more broadly in the subsequent part of this paper.

Taxation of various forms of the banking sector is a ubiquitous measure in all parts of the world. But the taxation methods vary. However, it needs to be highlighted that the form adopted by the Polish legislator is among the most stringent and burdensome to the sector. While analysing issues arising from this tax, it is impossible not to mention, however briefly, the fiscal policy. The programme proposed by the government presumes a growth in social expenditure, the coverage of which needs to be guaranteed by the state budget. Otherwise, the subsequent deficit and the growing public debt will surpass the thresholds specified in Article 216 of the Constitution of the Republic of Poland, and Art. 86 of the Public Finance Act (hereinafter, the P.F.A). It is also worth recalling Article 126 of the Treaty of the Functioning of the European Union, the provisions of which prevent excessive deficit. Both the state budget's greater demand for financial resources, and the new types of taxation therefore implemented should be justified appropriately. The recitals to the Bank Tax Act, state directly that this legal document responds to the state budget's increasing demand for funds to perform the government's programmes. The principle of social justice is recalled, as well as the fact the society was struck by tax rates on commodities and services raised in 2011, as the burden of such

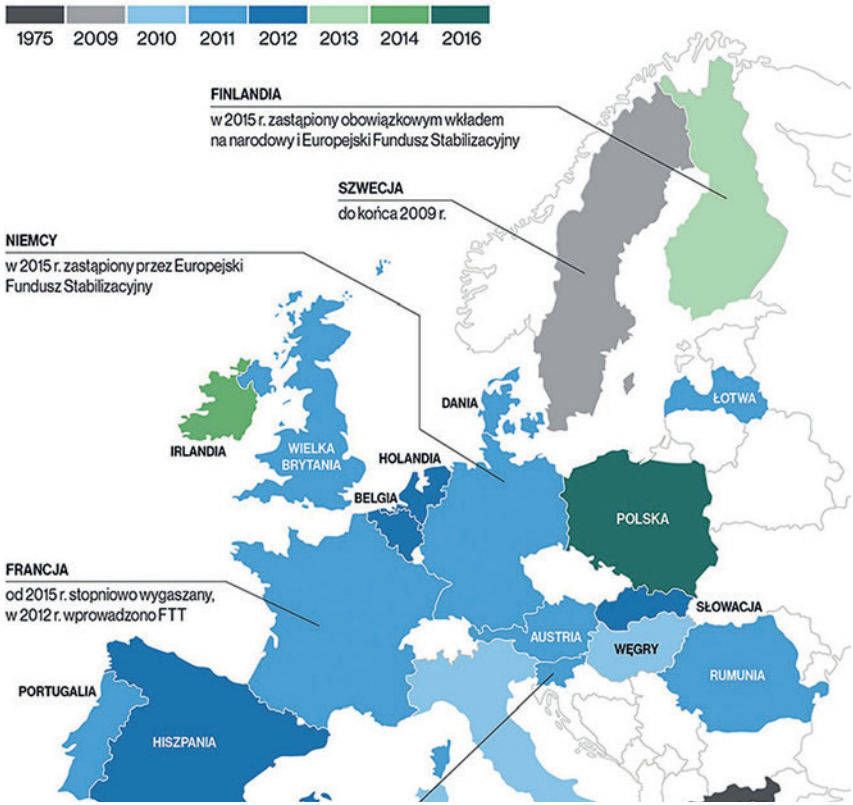
3 Other taxed entities are domestic insurers (15,8 %) and different entities (0,7 %) according to information given by Supreme Audit Office on tax collection from financial institutions, registration number: 5/2018/P/17/012/KBF.

taxes is naturally transferred onto the general public. The new tax was estimated to generate revenue comparable to the income earned by the state budget if a VAT rate was raised by 1 per cent point. It should therefore equalise the burden of maintaining the state budget between the society and the sector of business enterprises. This line of reasoning raises doubts. Despite obvious arguments like implementing state policy and combining public and private interests it can also be seen as a kind of financial penalty (Juchniewicz, 2016: 77). A question arises as who will eventually carry the burden of the new tax stipulated by the provisions of the Bank Tax Act? The legislator, in Article 14, included a clause to protect clients of the financial sector from adverse consequences of this legal solution. Nevertheless, the clause only pertains to agreements done prior to the Bank Tax Act, coming into force. There is likelihood that in the future the actual burden will be shifted by the financial market institutions onto its clients. And this contradicts the assumption formulated in the preamble to the Bank Tax Act, implicating that the new tax will contribute to the burden imposed by the state budget's demand being shared more equally between the society and the business sector.

The essence of bank taxes is well known, and the number of states which have decided to additionally tax the financial market is high (including 21 EU member states). However, in the majority of cases, bank or quasi-bank taxes have been levied in response to the financial crisis started in 2007. They were to deter the banking sector from duplicating the past errors and from investing or entrusting money in a way that would exceed the normally accepted risk in this sector. In some cases, revenues from a similar bank tax in the EU states have been transferred to the central state budget, but there are also cases of countries like Belgium, Sweden, Slovakia or Germany, where these incomes supply a stabilisation fund and actually contribute to ensuring the stability of the financial sector (Wojciuk, 2017: 30). This tax was also supposed to reduce the instability of financial markets, and to limit high-risk operations conducted by banks or financial institutions (Martysz, Bartlewski, 2018: 103). In addition, it was assumed that potential revenues from the bank tax would set off the losses the states suffered during the crisis while trying to rescue the financial sector. (Keen, 2011: 1) And it was actually the market

of subprime credits that turned to be the chief perpetrator of the global crisis (Gierczyńska, Wojciechowska, 2009: 9–16). Apart from imposing certain prudential norms, the institution of new taxation also aimed to assist the economies of the EU states in recovering, quickly as possible, the condition which they had had before the crisis struck (Kil, Ślusarczyk, 2014: 124–133). Some of the new taxes were envisaged to be transient obligations. The Polish legislator decided to levy the bank tax 4 years later than most of the member states that had opted for this solution (16 out of 21 implemented the reforms in 2010–2012, cf. fig. 1).

Fig. 1: Bank tax in EU states



Source: https://www.nik.gov.pl/aktualnosci/pobor-podatku-od-instytucji-finansowych.html [cit. 20 Februray 2019].

However, the recitals of the Bank Tax Act, concerning the 'bank tax' do not provide the arguments similar to the ones given by other EU states. (Merza, Overescha, Wamserb, 2017: 20) An explanation can be sought in the fact that this would be another burden to the banking sector arising from the same reason, as the contributions to the Bank Indemnity Fund are gradually increasing. These are defined quarterly by the Council of the Bank Indemnity Fund, pursuant to the provisions of the Act on the Bank Indemnity Fund, Deposit Guarantee Scheme and Resolution, of 10 June 2016 (hereinafter B.I.F. Act).

The bank tax can be attributed three main functions. One is to recuperate the costs incurred by the states during the crisis and to accumulate funds in case of subsequent crises. Another function of the tax is to improve the stability of the financial sector. (Hodula, Pfeifer, 2018: 196) It can be done by enforcing the banks to reduce the risk. (Brunnermeier, 2009: 77) The last role of the bank tax is its fiscal function, whose aim is to generate more budgetary revenue (Siudek, 2011: 64).

In practice, all EU state which has decided to implement post-crisis taxes has adopted highly different models and taxation objects. (Schőn, 2016: 425) The tax can be levied according to the balance total value, value of net assets, value of liabilities, or value of total capital. The Polish model is closest to the Hungarian one, implemented as early as in 2010, where the taxable base is the value of net assets. The Hungarian model is progressive. The assumed tax rate is 0,15 % of the above assets, but for larger institutions with assets above 50 thousand million HUF, the rate grows by nearly three-fold, to 0,53 % of the net asset value. According to the estimates of the Ministry of Finance, this is the highest tax rate in the EU. When the Polish and Hungarian versions of bank tax are compared, it occurs that the latter is much more stringent. The Hungarian model does not assure any value of tax-free assets, but only differentiates the tax rate. In Poland, taxes are levied only on these banks in which the value of assets exceeded 4 thousand million PLN (about 928,5 thousand million €). A similar model of tax exemption has been implemented in Austria, with the threshold similar to the Polish, i.e. set at 1 thousand million €. This similarity was brought to light by the Polish Ministry of Finance in the justification of the Bank

Tax Act. In the Polish law, the threshold of 4 thousand million PLN was substantiated by the necessity to encourage the development of the sector, and by the intention of relieving the tax burden from institutions which positively affect the competition on the market. The Hungarian version, in turn, covers all objects. Should our analysis conclude at this point, we might even suggest that the Polish model is extremely subtle and puts burden only on the biggest actors on a given market. Similar models of taxation based on assets have been implemented in Finland or France.

The projection of revenues presented in the justification of the Act showed that the proposed tax would generate annual revenue to the state budget of about 6,5–7 thousand million PLN (between 1 508 and 1 624 thousand million €). The projected income was calculated at the originally planned tax rate, which was 0,0325 %, but the actual rate in the Act passed after amendments is 0,0366 % (Art. 7). This means that the above revenue level should be higher by ca 12,5 %, and range between 7,4 and 7,87 thousand million PLN (between 1 717 and 1 826 thousand million €). Three years after the bank tax entered into force, it is known that the assumed level of incomes is unattainable, at least for the time being. The results of the audit performed by the Supreme Audit Office (the Polish acronym: NIK) concerning the collection of the tax levied on certain financial institutions demonstrate clearly that the authors of the Act, in its justification, cited data which can be now seen as overestimated. Since the time the Act came into force until the end of 2016, the bank tax generated no more than 3,5 thousand million PLN (about 812 thousand million €) a year on average, which is about 54 % of the lower threshold revenue assumed in the Act's justification. However, the Supreme Audit Court emphasises that the revenue in 2017 equalled 4,3 thousand million PLN (about 998 thousand million €), and this was a better outcome than in the preceding year, and higher than planned (110,3 % of the planned revenue).

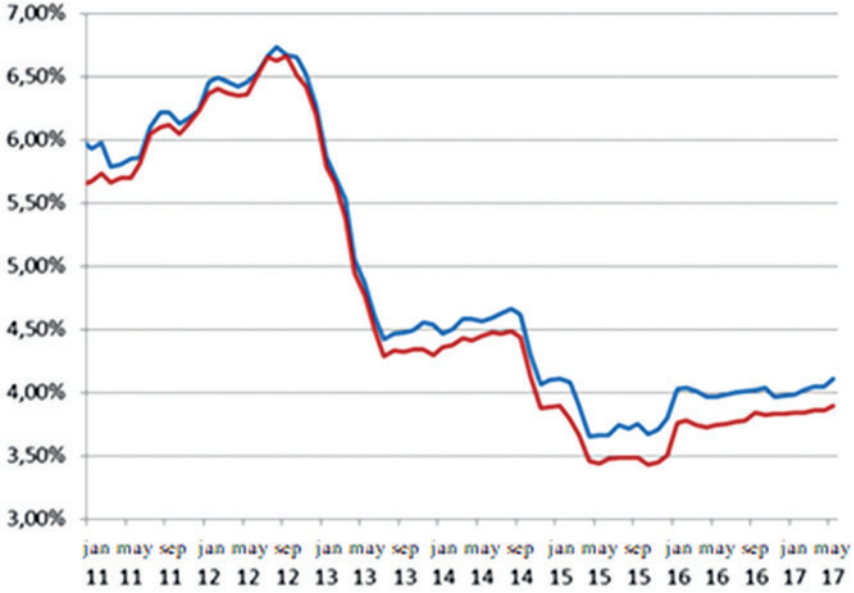
The revenue from the tax in 2018 is merely an estimate, but it is expected that it would not fall below 4,4 thousand million PLN (1 021 thousand million €). In the two years, 2016 and 2017, there were about 90 institutions from the broadly understood financial market that were obliged to pay the tax. This, however, does not mean that their number is constant. In fact,

it fluctuated over the analysed period of time from 79 to 82 in 2016 and from 75 to 81 in 2017, depending on a month. The Act had a demonstrable effect on the demand of financial institutions for treasury bonds, which when purchased, as stipulated in Art. 5 paragraphs 9, can be deducted from the taxation base, and this certainly is a positive consequence of the new regulations. The banks' investment in the Treasury bonds increased over a year and a half (from January 2016) by 72 thousand million PLN (16 713 thousand million €), i.e. by 40 %. Nonetheless, according to the Supreme Audit Court, this situation does not raise any concerns and the measures taken by the banks bear no semblance to tax optimisation. The tax collectability is 100 % and no long-term due taxes are observed, hence there has been no need to instigate administrative procedures to collected due taxes. The monthly revenue from the bank tax varies between months, but typically lies in the range of 330–370 million PLN (76–85 million €). The total revenue from the tax in 2016 was 1,1 % of the state's revenue and rose to 1,3 % in 2017. In order to ensure the high effectiveness of tax collection, it was necessary to amend the Act with specific interpretations issued by the Ministry of Finance.

Bearing in mind the revenues which the bank tax has contributed to the state budget, it is advisable to review the impact of this tax on taxpayers. The starting point will be the year 2015, and the results achieved by the banking sector in that year. It emerges that the net profit of the banks, which was 11,2 thousand million PLN (2,6 thousand million €) in 2015, increased to 13,9 thousand million PLN (3,2 thousand million €) in 2016 (which corresponds to an improvement of about 24 %) and equalled 13,6 thousand million PLN (3,1 thousand million €) in 2017 (by *ca* 22 % more than in 2015). The difference which was 2,7 thousand million PLN (626 thousand million € in 2016) and 2,4 thousand million PLN (557 thousand million € in 2017), respectively, compensates for a considerable part of the tax due in every year. Thus, the bleak scenario predicted for individual clients did not happen. Contrary to the expectations, the cost of serving accounts of natural persons, following the dynamic growth in 2014 and 2015, has stabilised or even declined. This, in turn, means that banks are not searching for sources of financing the due tax in this section of their offer. The same,

unfortunately, cannot be said about the market of mortgage loans. The rate of mortgage credits has risen distinctly since January 2016, despite the stability of interest rates, which are determined by the Monetary Policy Council, and the absence of any change in the level of thereof since 2015.

Fig. 2: Average interest rate in mortgage credits taken in Poland



Source: Report of Metrohouse and Expander [cit. 15 May 2018].

Insofar as the current situation of low interest rates of the Polish National Bank (NBP) continues, the above policy of banks can be considered as neutral to clients; yet, any amendment to the Monetary Policy Council's strategy may stimulate a significant rise in loan payments for the credit-takers.

Other measures are taken by the banking sector as well, to cover the cost of the bank tax. Without doubt, the sector is to largely strengthen by the good situation in the housing market and by increasing investments. Meanwhile, the banks have accomplished certain cost restructuring and optimising. The enforcement of the bank tax has affected adversely the labour market in the banking sector, where the employment has decreased (by nearly 4,5 thousand persons) and over 1,000 branch offices have closed down.

The new fiscal obligation imposed on the banking sector, which – compared to the EU - even without the bank tax is subjected to heavy burden, forced the banks' executive management and boards of directors to take action. Although not all bank products have been affected, it is justifiable to claim that the banks have mostly taken this new burden on their shoulders and decided to cover the obligations from their profits. Today, they are also sharing this burden with their clients.

3 The structure of the Act and the construction of the tax payable by certain financial institutions

The Act on Taxation of Certain Financial Institutions is composed of seven chapters, and the tax was constructed in accordance with the tax construction elements. The following were defined: the subject, the object, the tax base, tax rate, exemptions and exclusions. Our analysis of the issued interpretations and court rulings enables us to conclude that the determination of the object scope and establishment of the taxation base are particularly complicated in the light of the Act.

3.1 The scope of the tax entity

The entities covered with the new tax are determined in Article 4 of the Bank Tax Act. The catalogue presented in the Bank Tax Act suggests that taxable subjects divide into three groups: the banking sector (including quasi-banks), the insurance sector (which is a substantial deviation from the construction of the bank tax in other European countries), and the loan sector. Thus, the taxation obligation applies to national banks, branches of foreign banks, and branches of savings and credit institutions as defined by the Bank Law of 29 August 1997, cooperative savings and credit unions (SKOK) as defined by the Act on Cooperative Savings and Credit Unions, of 5 November 2009, national insurance companies, national reinsurance companies branches of foreign insurance and foreign reinsurance companies as defined by the Act on Insurance and Reinsurance, of 11 September 2015, as well as loan companies as defined by the Act on Consumer Credit, of 12 May 2011.

The Act on Taxation of Certain Financial Institutions provides a separate definition of a taxpayer, identified by belonging to one of the groups enumerated in Article 4. Consequently, the criteria for defining taxpayers in income taxation regulations are not applicable, and neither is the limited and unlimited tax obligation.

The tax was levied on the institutions selected by the legislator, but not on all subjects operating in the financial sector, which may give rise to certain doubts on the ground of equality and universality of taxation.[4] For instance, the cooperative savings and credit unions (SKOKs) need not bother about the tax because of the structure of their assets. The report published by the Main Statistical Office in Poland (GUS) in 2017 shows that the total worth of the assets owned by SKOKs (40 unions were submitted to the analysis) was over 11,25 thousand million PLN (2 611 thousand million €). In the current construction of statutory tax exemptions, all SKOKs and Cooperative Bank have avoided paying the bank tax, although if not for the additional statutory exemptions, the largest active cooperative savings and credit union, i.e. Stefczyk SKOK, would have had to pay it (Central Statistical Office, Warsaw, on 16/10/2017. Financial results of cooperative savings and credit unions in 2016).

The Polish bank tax, contrary to other taxes of this type implemented in the EU member states, covers the banking sector as well as the loan and insurance sectors. The taxation scheme for the insurance sector appears particularly different from the solutions adopted in other countries. (Merza, Overescha, Wamser, 2017: 24) In most European countries, there is a special tax levied on insurance contributions.

The bank tax in Poland is not levied on foreign insurance companies from the European Union member states operating in Poland, which complies with the freedom to provide insurance services, or on banks conducting transborder banking activities. In the justification to the Act's draft, it was implicated that taxation of the above subjects would be excessively complicated.

4 Currently there is only one institution which is *ex lege* excluded from the taxpayers set. Talking about Bank of National Economy. It seems to be a logical move of the legislator because its created of 100 % state capital and it would be unjustifiable to tax states own property.

Pursuant to Article 11, exemption from the bank tax is also granted to subjects for which the Financial Supervision Authority in Poland has passed a decision of dissolution, suspension of activity or bankruptcy, or for which a board of receivers has been appointed. Similar regulations apply to insurance companies and SKOKs.

The legislator decided to exclude the Bank of National Economy (Bank Gospodarstwa Krajowego, polish acronym: BGK), or any other state banks that will be established in the future, from the scope of taxable subjects. The tax exemption granted to state banks arises from the essence of their operations, where the main aim is not commercial activity. (Frych, 2017: 129) Noteworthy, the exemption constructed in this way means that even a possible strictly speaking commercial activity of state banks will not give rise to a tax obligation. Another reason why the legislator decided to exempt state banks is the fact that these banks are supplied assists transferred to them by the Treasury of the State, and therefore their taxation would entail a tax being levied on the state's financial assists and the revenue from this tax being paid to the state budget. (Keen, 2011: 21) Moreover, this exemption of state institutions inscribes itself into the construction of any tax and seems to be a rational measure.

While analysing the first of the issued interpretations and rulings of administrative courts of law concerning the tax on certain financial institutions, attention should be drawn to numerous doubts pertaining to the subject scope – and particularly with respect to loan institutions.

In one of the applications for individual interpretation, a company engaged in the trade of liabilities submitted a query to a taxation organ whether they should be considered a taxpayer of the new tax, considering the fact that although their register of business activity contains the entry 64.92.Z. – other forms of credit provision, the company has not performed these services after the Act entered into force.

The Provincial Administrative Law Court (WSA), in its ruling of 14 March 2017, ref.: I SA/Gl 1549/16, confirmed the opinion of the interpreting organ, indicating that the mere fact of terminating consumer loan agreements within the meaning of the Act on Consumer Credit does not entail a loss of the status of a loan institution by the company, in accordance

with Article 5 paragraph 2a of the Act on Taxation of Certain Financial Institutions. The WSA draws attention to the fact that although the company does not offer consumer credits to natural persons, this does not preclude a possibility that it may do so at any time in the future. This possibility is implicated by the profile of the company's economic activity and its actual status presented by the applicant.

On the basis of the above ruling, it needs to be concluded that a motion to dissolve credit agreements alone does not alter the status of a company as a credit provider, and such companies should be considered as payers of the tax on certain financial institutions.

Another problem that needed interpretation was the qualification of a taxpayer according to the form of business activity. In an individual interpretation dated on 11 May 2017, ref.: 2461-IBPB-1-3.4510.58.2017.2.IZ, the Director of the National Revenue Information replied to a query addressed by a company, which wished to resolve whether it could be considered a payer of the tax on certain financial institutions if it conducted business as a partnership limited by shares. In the justification to the query, the company explained that a partnership limited by shares cannot be considered to be a loan-providing institution according to the Act on Consumer Credit, which entails a consequence such as the lack of justification to consider it as a taxpayer of the bank tax. The interpretative body completely agreed with the company's opinion.

Having an adequate legal form as a requisite for being recognised as a player of the tax on certain financial institutions is also confirmed by the Minister of Finances in the General Interpretation, stating that "*In this matter it is justified to refer to the aforementioned Act on Consumer Credit, which in detail defines the form and regulations applying to the operation of loan institutions. It is worth emphasising that the above Act contains the requirement of having an appropriate legal form and submitting a declaration that the business entity intends to conduct its business activity in the scope of provision of consumer credits as a loan institution*."

Additionally, in the General Interpretation the Minister of Finances explained that the bank tax is not levied on companies which offer loans to own employees, e.g. in compliance with the regulations of the Company Social Benefits Fund. (General Interpretation of the Minister of Finance,

No. PK1.8201.1.2016 of 3 March 2016 on the application of the provisions of the Act on tax on certain financial institutions by tax authorities and fiscal control authorities.)

The dependence and co-dependence between taxpayers, however, was not explained on the ground of the Act. According to the General Interpretation of the Minister of Finances of 3 March 2016, concerning the application of the provisions of the Act by revenue bodies and revenue auditing bodies (ref.: PK1.8201.1.2016), the terms of dependence and co-dependence should be interpreted in compliance with the Act on Accountancy or the International Accountancy Standards – depending on what policy of accountancy or accountancy rules a taxpayer has adopted. The confirmation of this interpretation can be found in the General Interpretation of the Ministry of Finances concerning the implementation of the provisions of the Act by revenue bodies and revenue auditing bodies (Rationale for the draft law on the tax on certain financial institutions, print no. 75, of 3.12.2015: 8).

Additionally, in line with Article 5 paragraph 2 of the Act, in the case of institutions other than banks, the tax is levied only on the assets in excess of 2 thousand million PLN (464 thousand million €). The surplus of the assets above this threshold, in the case of subjects dependent or co-dependent directly or indirectly on one subject or a group of mutually associated subjects, is calculated jointly for the whole capital group (Marszelewski, 2016: 104) The purpose of this construction is primarily to prevent tax evasion by artificial divisions of mutually connected entities.

3.2 Scope object of tax and the taxable base

The bank tax should be classified as a property tax, i.e. a tax payable on the owned assets or surplus of these assets. (Furman, 2017: 76)

Pursuant to Article 3 of the Bank Tax Act, the object of taxation with the tax on certain financial institutions is the assets of the subjects which are taxpayers of this tax. The taxable sum was adjusted to the category of a taxpayer.

With regard of taxpayers such as national banks, branches of foreign banks, branches of credit unions or cooperative savings and credit unions, the taxable amount is the surplus worth of the taxpayer's assets calculated from a statement of turnover and balance prepared for the last day of a month based on entries in the general ledger of accounts or accounting standards applied by the taxpayer pursuant to Article 2 paragraph 3 of this Act, which is above 4 thousand million PLN (Bronżewska, Majdanowski, 2016: 17).

The Bank Tax Act makes a provision to exempt a balance sum of the value no more than 4 thousand million PLN (about 928,5 thousand million €). This exemption aims to protect financial institutions which have a positive influence on the competition on the market and which, if submitted to the tax, would suffer negative consequences.

With respect to taxpayers such as national insurance companies, national reinsurance companies, branches of foreign insurance companies and foreign reinsurance companies, as well as the main branches of foreign insurance company branches, the taxable amount is the surplus of the taxpayer's total assets calculated from a statement of turnover and balance set for the last day of a month according to the entries in the general ledger of accounts over the amount of 2 thousand million PLN (464 thousand million €).

The taxable amount was also indicated separately for loan companies, where it is the surplus of the sum of the worth of a taxpayer's assets calculated from a statement of turnover and balance set for the last day of a month according to the entries in the main ledger of accounts, in compliance with the Bank Tax Act, on Accountancy, of 29 September 1994, or the accountancy standards adopted by the taxpayer in accordance with Article 2 paragraph 3 of the mentioned Bank Tax Act, – over the sum of 200 million PLN (46 thousand million €). This amount is calculated in total for all taxpayers dependent or co-dependent on one subject or a group of mutually connected subjects (Individual interpretation of the Director of the Tax Administration Chamber in Warsaw of 10 August 2016, IPPB3/4510-539/16-5/MS).

Thus, by defining the taxable amount the legislator referred to the surplus of the taxpayer's total assets resulting from the statement of turnover and balances established on the last day of the month (Individual interpretation

of the Director of the Tax Administration Chamber in Warsaw of 10 August 2016, IPPB3/4510-539/16-5/MS) The above definition of the taxable base leads to numerous interpretation disputes, because the assets can be presented a gross or net worth (Polish Bank Association, Opinion on the draft law on the tax on certain financial institutions addressed to the Budget and Public Finance Committee of the Senate of the Republic of Poland, 28/12/2014: 5).

The Minister of Finances, in the General Interpretation, indicated that pursuant to Article 18 of the Act on Accountancy, of 29 September 1994, entities keeping accounting books are obligated to prepare at the end of each reporting period, at least at the end of each month, a statement of account turnover and account balances including:

- Symbols or names of accounts;
- balances of accounts as on the day the accounting ledgers are opened, turnovers for the reporting period and incrementally since the beginning of the turnover year, and balances at the end of the reporting period;
- the sum of balances as on the day the accounting ledgers are opened, turnovers for the reporting period and incrementally since the beginning of the turnover year, and balances at the end of the reporting period.

The Minister of Finances indicated that when determining the taxable amount the taxpayers are obliged to take into account the worth of the assets calculated from the balances of all the accounts listed above.

In its construction, the tax was based on self-calculation. Pursuant to Article 8 paragraph 1, taxpayers are obligated, without being called by the revenue authorities, to submit to the locally competent revenue office completed tax forms, and to calculate and pay the tax due to the account of the competent revenue office – for monthly settlement periods, no later than on 25 day of the month consecutive to the month for which the tax is due.

The Act on Taxation of Certain Financial Institutions identifies the competent revenue body as the head of the internal revenue office locally competent with respect to the seat of the taxpayer's company or company branch. When it is impossible to identify the competent revenue office, the Head of the Second Internal Revenue Office in Warsaw-Downtown is considered to perform this role.

Pursuant to Article 7 of the Act on Taxation of Certain Financial Institutions, the tax in question equals 0,0366 % of the taxable base monthly.

4 Conclusion

After analyzing the impact of the new tax on various spheres of the economy, what should be noted that despite the relatively low rate of this tax, **it has not remained neutral and unnoticeable for the participants of the financial market.**

It directly touched commercial banks and insurance institution. Indirectly it hit the clients of the banking and insurance market. Although the reaction may be initiated with a delay dependent on the organs of the National Bank of Poland. Therefore, the challenge for both, National Bank of Poland, as well as polish government will be to anticipate the raising of the interest rates in advance. The fact of raising, without any doubt, will have to come at a time of intense economic growth. This will turn in further reduction of new bank loans granted and will inhibit economic growth. As mentioned in the text, as a result of the new tax the number of new loans taken has decreased and a possible increase of interest rate will only deepen this effect.

Concerns about the effects of the new tax turned out to be real, such as a decrease in the number of new loans taken in the enterprise sector. This inhibits the revenues to the state budget. Banks are focusing on the most-profitable loans, while limiting deposit rates (deposit rates dropped by 15 % year-on-year)

Bank tax in its current form is certainly not optimal. It threatens the competitiveness of not only the banking sector itself, as it significantly stops the expansion of the polish banking sector. Due to the high costs of loans, the attractiveness of Polish enterprises in comparison to the enterprises from eurozone decreases. This is where the role of the state should be noticed waiting for the appropriate intervention. This may give a breath to the banking sector and the whole enterprise sector in order to use the full of its development potential.

An unquestionable surprise is the lack of noticeable increase in fees and commission in retail banking, which initially seemed to be the first potential

source of coverage of the new costs related to the new burden. Contrary to expectations, banks still offer cheap, sometimes free of charge banking for individuals. In this case, the absence of the effects of the new tax should be considered as positive. The European Central Bank fears regarding the destabilization of the entire banking sector in Poland have also failed.

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Fiscal and Balance Sheet Effects of the Splitting up of Sources of Revenue in Corporate Income Tax

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Abstract

This contribution concerns the issue of the similarities of splitting up sources of income in corporate income tax and the operating activities and financial revenues appearing in the profit and loss account. The main aim of the article is to confirm or disprove the hypothesis that the introduction of provisions distinguishing tax revenues from capital gains means that norms of balance sheet law are recognized by tax law as forming a tax factual state. Author uses normative and dogmatic methodology to prove lack of complete autonomy between regulation of tax law and balance sheet law.

Keywords: Corporate Income Tax; Balance Sheet; Sources of Revenue.

JEL Classification: H25; H26; K34.

1 Introduction

As of 1 January 2018, source of revenues from capital gains was distinguished[2] (Journal of Laws of 2017, item 2175) under the Corporate Income Tax Act[3] (Journal of Laws of 1992 no. 21 item 86, as amended). The analogue of this source of revenues in balance sheet law is the financial income that had not been distinguished in tax regulations before. Therefore, revenues from capital gains were treated as tantamount to operating revenues. Currently, such definition of sources of revenue in the tax law affects

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2 The amendment was introduced by the Act of 27 October 2017 on the amendment of the Act on personal income tax, Act on corporate income tax and the Act on flat-rate income tax on selected incomes earned by individuals (Journal of Laws of 2017, item 2175).

3 Act of 15 February 1992 on the Corporate Income Tax (Journal of Laws of 1992 no. 21 item 86, as amended), hereinafter: the CIT Act.

the method of determining the costs of revenues. A taxpayer which earns operating and financial income is therefore not entitled to combine costs related to capital gains with operating expenses[4] (Journal of Laws of 1994 no. 121 item 591, as amended).

The aim of this study is to show the similarities between the distinction of income from capital gains in personal income tax and the revenues from operating activities and financial revenues appearing in the profit and loss account. It should be assumed that the relationship between tax legislation and balance sheet regulations should not rely entirely on the rule of autonomy. The introduction of provisions distinguishing tax revenues from capital gains means that norms of balance sheet law are now recognized by tax law as forming a tax factual state. The content of provisions adopted by the tax legislation proponents, which qualify tax revenues in this way, may be aimed at simplifying the method of calculating the tax base.

2 Autonomy of regulation of tax law and balance sheet law

The terms "income", "cost" and "financial result" are used not only in tax legislation, but also in the Act on accounting[5] (Journal of Laws of 1994 no. 121 item 591, as amended). However, these terms should not be deemed the same. The distinction between the meaning of these terms results from autonomy of tax law and balance sheet law. This in turn stems from different purposes and functions of both branches of law, so the difference exists at the level of general principles[6] (Walińska, 2016: 90). Accounting is primarily supposed to provide information on the business run by a particular entity. Therefore, accounting records kept in compliance with accounting laws are supposed to provide, as a rule, a true and fair view of the financial situation of the entity (Walińska, 2010: 20; Jarugowa, 1997: 12). The economic information thus obtained serve as tool of assessment of economic

4 Operating activity, i.e. core business activity, depend on the enterprise's profile.

5 Act of 29 September 1994 on accounting (Journal of Laws of 1994 no. 121 item 591, as amended), hereinafter: the Accounting Act.

6 Several groups of accounting principles may be distinguished: fundamental principles (the accrual principle and the continuity principle), statutory accounting principles, general principles and specific principles.

performance and planning. On the other hand, tax law primarily pursues its fiscal objective, implemented by imposing mandatory levies for the public-law authority (Hejnar, 2011: 13; Kaplow, 1998: 61–83).

The literature on the subject provides three basic concepts defining the mutual relation between balance sheet law and tax law[7] (Litwińczuk, 1995: 163). First, a relationship based on the complete mutual autonomy of both branches of law. According to its assumptions, the tax result is determined separately and irrespective of the accounting result. The second concept is the concept of identical regulation of both branches of law. The adoption of this concept would constitute a significant simplification, because it would not necessarily require economic operators to keep separate records of financial operations solely for tax purposes. Third, the concept of interdependence of both regulations, with the assumption of temporary prevalence of either balance sheet law or tax law. To accept it, it would be necessary to conclude that taxable income and balance sheet profit are two separate economic and legal categories[8] (Olchowicz, 2011: 66). However, taxable income would be determined based on the amount recognised in the financial statements. It would then be appropriate to revise the costs which under tax laws are not regarded as revenue costs, and the revenues exempt from taxation[9] (Scheffler, 2011; Hennrichs, 2015: 500).

The Polish legal system uses the concept of a complete separation between both regulations. However, it is not implemented in a coherent way. Under the Tax Ordinance Act[10] (Journal of Laws of 1997 no. 137 item 926, as amended), accounts that are kept reliably and correctly may constitute evidence in tax proceedings[11] (Hanusz, 2004). However, under the provisions of Article 9 of the CIT Act, taxpayers are required to keep accounting records in accordance with separate provisions, in such a way as to determine

7 This distinction is widely accepted in the literature on the subject.

8 The concept of interdependence of regulation of tax law and balance sheet law applied in the Polish law in the inter-war period.

9 In German law the so-called authoritative principle (*Maßgeblichkeitsprinzip*) applies, which means that commercial balance sheet must form a basis for the calculation of fiscal burden.

10 Act of 29 August 1997 – Tax Ordinance Act (Journal of Laws of 1997 no. 137 item 926, as amended), hereinafter: TOA.

11 Cf. Article 193 TOA.

the amount of income (loss), taxable base and amount of tax due (Supreme Administrative Court: II FSK 487/13). The Act on corporate income tax therefore clearly refer to norms resulting from the provisions of the Act on accounting. However, the provisions of balance-sheet law are only relevant to the extent specified by the provisions of tax law. Under the regulation referred to in above, only the provisions of tax law may provide the basis for considering a given appropriation or expenditure as a taxable revenue or revenue cost. Clear references to the provisions of the Accounting Act on accounting are therefore unambiguous (Supreme Administrative Court: II FSK 182/14, II FSK 1731/08, II FSK 3359/14). Tax authorities verify whether the accounting records are in conformity with the facts and whether the legal events recorded therein are properly qualified (Wencel, 2018: 477).

Balance sheet law plays a secondary role in this case, by providing tools for calculating fiscal burdens. The content of Article 9 of the CIT Act provides the basis for the same record system for accounting and taxation purposes (Pęk, 2013: 166). However, differences in determining the financial result and taxable income do not exclude their similarity in accounting terms. This relationship is reflected in the content of the provisions of tax law and balance sheet law (Chernikova, Gorosh, 2017: 281–288). The mutual adjustment of fiscal and balance sheet provisions is necessary in order to blur the border between the method of calculation of the accounting and tax result (Litwińczuk, 1995: 170).

3 The essence of distinguishing the revenue from capital gains

The amendment to the Act on corporate income tax has led to the separation of the source of revenue in the form of capital gains, and thus to the separation of revenue coming from this source from the other taxpayer's income. The revenue from capital gains must therefore be distinguished from the other revenues earned by the taxpayer. The purpose of such a change was to stop

the deliberate creation of a tax loss by CIT-taxable entities in order to reduce the income earned from the core business activity[12].

The tax legislature refrained from defining income from capital gains by classic definition. Article 7b of the CIT Act contains only a list of revenues that qualify in this category[13]. The catalogue in question is of a complete nature. According to the provision mentioned above, revenue from capital gains include revenue in the revenue actually derived from the share in profits of a legal person. This refers to, but is not limited to, dividends, revenues from redemption of shares or stocks, or revenue earned as a result of transformation, merger or division of corporate entities. Moreover, revenue from capital gains includes revenues arising from making a contribution in kind to a legal person or a company, the revenue from disposal of receivables previously acquired by the taxpayer and receivables deriving from revenue classified as capital gains, and revenue from certain property rights. It is necessary to mention here copyright or related proprietary rights and licences[14] (Regional Administrative Court of Rzeszów: I Sa/Rz 740/18; Regional Administrative Court of Olsztyn: I Sa/Ol 461/18; Opoka, Thedy, 2018; Koleśnik, 2018: 8) and exchanged of a virtual currency for another medium of payment, goods, service, or a property right other than virtual currency, or to settle other liabilities with a virtual currency[15] (Journal of Laws of 2018, item 2193). From the point of view of legislative technique, the catalogue of sources of revenue from capital is essentially a denotative definition. It enumerates the constituent elements of the scope, while meeting the criterion of clarity and communication[16] (Journal of Laws of 2002 item 908; Dębska, 2013).

12 The explanatory note to the draft Act of 4 October 2017 on the amendment of the Act on personal income tax, Act on corporate income tax and the Act on flat-rate income tax on selected incomes earned by individuals.

13 It is wider than the catalogue of revenues from profits earned by legal persons, which until 1 January 2018 was contained in in Article 10 of the CIT Act.

14 The issue of disposal of licences and copyright has already been subject to judicial review.

15 Added under the the Act of 23 October 2018 on the amendment of the Act on personal income tax, Act on corporate income tax, Tax ordinance Act and certain other laws (Journal of Laws of 2018, item 2193).

16 Cf. § 153 paragraph 1 of the Ordinance of the President of the Council of Ministers on the "Rules of Legislative Methodology" of 20 June 2002 (Journal of Laws of 2002 No. 100, item 908), hereinafter RLM.

Using the achievements of accounting studies, the second category of revenue can be defined as operating revenue (Małecki, Mazurkiewicz, 2018). In accordance with the provisions of the Act on corporate income tax, taxpayers are required to qualify the revenues earned in one of the categories. This will, in turn, result in the determination of the costs of obtaining revenue and the possibility of settling the tax loss. Taxable persons who obtain revenue from both economic activity and therefore operational activities within the meaning of the Act on accounting as from capital sources are therefore entitled to recognise the costs of obtaining revenue only for the corresponding Income categories[17] (Małecki, Mazurkiewicz, 2018). *A contrario*, taxpayers are not entitled to deduct the cost of capital gains revenue from operating revenue.

If revenue has been earned at both sources, then the aggregate revenue from both sources is taxable. However, if a loss is incurred in one of the sources of revenue, then the taxpayer is not entitled to deduct this amount from the income obtained from the second source of revenue. However, the taxpayer may reduce the income from that source of revenue within five consecutive fiscal years. However, the amount of such a reduction in any of these years may not exceed fifty percent of the amount of the loss[18] (Waślicki, 2007: 29).

4 Categories of revenue presented in financial statements

According to the norm set out in Article 42 of the Accounting Act, in entities other than banks, insurance and reinsurance companies, the net financial result of the entity consist of the operating result and the result of financial operations. In addition, the consolidated financial statements include compulsory encumbrances on the financial result for income tax imposed on the entity, and payments deemed tantamount to the above under separate provisions. Property taxes, tax on goods and services and income taxes may constitute

17 Cf. Article 15 paragraph 1 of the CIT Act.

18 Cf. Opinion of the Legislative Council at the President of the Council of Ministers concerning the draft Act of 22 September 2017 on the amendment of the Act on personal income tax, Act on corporate income tax and the Act on flat-rate income tax on selected incomes earned by individuals.

in the accounting system respectively a cost, settlement or encumbrance on the financial result (Walińska, 2016; Gierusz: 2010: 175). Therefore, they are also presented accordingly in financial statements (Iwin-Garzyńska, 2014: 90–91).

The tax result and accounting result are determined according to the same general rule, namely by deducting costs from the revenue (Olchowicz, 2011: 64). According to the rules of balance sheet law, costs should be attributed to a relevant group of revenues, i.e. related to operating or financial activities (Czubakowska, 2016: 370; Waślicki, 2007). Thus, the financial result shown in the accounting books covers the operating result and the result of financial operations. At the same time, it should be noted that revenues from operating activities include those achieved as a result of the core business (Kondratowicz, 2006: 47). This should be understood as revenue from the sale of products, goods and materials, considering subsidies, discounts, rebates and other increases or decreases, without value added tax and other taxes directly related to sales turnover[19].

In addition, under the Accounting Act there is a category of revenues from other operating activities that was neither defined explicitly nor by enumeration. These are revenues indirectly related to the business run by the entity and characterized by diversity and volatility (Seredyński, Szaruga, 2015: 520). Financial revenues include, in accordance with the provision of art. 42 paragraph 3 of the Accounting Act, revenues from dividends, including shares in profits, interest, gains on sale and revaluation of investments, excluding investments in real estate and intangible assets and other non-financial investments, profit from disbursement of financial assets, or surplus resulting from positive currency exchange differences over negative ones (Michalak, 2018).

5 Final remarks

Differences in the determination of the financial result and tax result stem from different recognition of revenues and costs in tax law as compared to balance sheet law. Positive or negative differences can be distinguished, depending on whether the accounting result is higher or lower than the tax result (Olchowicz, 2011: 205). In accordance with the principle of commensurability,

19 Cf. Article 42 paragraph 2 of the Accounting Act.

which is the embodiment of the accrual principle, financial result depends on revenues earned in a given financial year and the corresponding costs[20]. Therefore, under the Accounting Act, commensurate should be those costs that contributed directly or indirectly to earning the revenues.

The demonstration of interrelation between the basis for income tax and the financial result presented in the profit and loss account boils down to the obligation of the taxpayer and tax authorities to use the information presented in accordance with balance sheet law. It should be stated that different methods of determining revenues, costs and results in tax and accounting terms make the tax law regulations too casuistic. Despite the differences resulting from the autonomy of tax and balance sheet law, the general principles remain common for determining both the tax and the accounting result.

The distinction of sources of revenue from capital gains under the Act on corporate income tax, and their similarity to financial revenues shown in the profit and loss account seems to be an important step on the way to unification of the accounting and balance sheet regulations. Although this will not be fully possible due to different purpose and functions of both branches of law, this process should be perceived as a link between the principles of determining the tax result and the principles of balance sheet law. Reducing the differences between the regulations of both branches of law is advantageous.

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Legal Status of Entrance Fees to National Parks and Nature Reserves Located on the Territory of the Republic of Poland

Małgorzata Ofiarska[1]

Abstract

The study addresses the legal status and principles for the introduction and charging of fees for entry into the area of national parks and nature reserves in Poland, which are forms of nature conservation and special areas. Its main purpose is to analyse and assess the normative material and the achievements of the doctrine of law concerning such fees. As a result of the conducted research it was shown that entrance fees to such special areas have a public law nature. They are introduced unilaterally by public administration bodies competent in matters of environmental protection (Minister for the Environment, director of a national park, regional director for environmental protection) by way of sovereign administrative acts. The hypothesis that entrance fees are a special type of environmental levies collected for the possibility of enjoying public facilities and proceeds from these fees are allocated to finance costs of implementation of public tasks in terms of nature conservation was verified positively. The study applied the dogmatic and legal method as dominant, and the empirical and analytical method as supplementary.

Keywords: Public Levy; Environmental Levy; National Park; Nature Reserve.

JEL Classification: H23; H83; K32.

1 Introduction

National parks and nature reserves are legal forms of nature conservation in Poland (Nature Conservation Act, hereinafter: NCA). A national park

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covers an area featuring specific environmental, scientific, social, cultural or educational values, whose size is not smaller than 1 000 ha, where all nature and landscape values are subject to conservation (NCA, Article 8). It is established in order to preserve biodiversity, resources, formations and elements of inanimate nature and landscape values, to restore the proper state of resources and elements of nature and to recreate distorted habitats (natural, plant, animal or fungi). According to the legal status as of 31 December 2018, there were 23 national parks in Poland (their total area covers approx. 1 % of the territory of the Republic of Poland). They are national legal persons forming part of the public finance sector in Poland (Public Finance Act, Article 9 section 14, hereinafter: PFA) which are established by the Council of Ministers by way of a decree. An act on creating a national park defines, i.a., its area and the course of its borderline.

A nature reserve covers areas preserved in their natural state or marginally altered, ecosystems, nature refuges and settlements, as well as other settlements (plant, animal and fungi) and also formations and elements of inanimate nature, featuring specific environmental, scientific and cultural attributes or landscape values (NCA, Article 13). Recognizing an area as a nature reserve proceeds by way of an act of local law in the form of an order from a regional director for environmental protection. According to information contained in the Central Register of Forms of Nature Conservation, 1 496 national reserves were distinguished in Poland covering in total 168 300 ha, which amounts to 0,54 % of the area of the country.

National parks and nature reserves are special areas created in order to protect various elements or values of the natural environment (Ofiarska, 2018: 338; Stelmasiak, 2013). The implementation of this function takes place through establishing orders or prohibitions, thus creating a national park or a nature reserve entails regulation of defined actions on a specified area (Ofiarska, 2000: 26). The operation of these special areas requires bearing expenses and one of the sources of financing them is entrance fees to national parks or nature reserves. The purpose of this study is to analyze and assess the normative material and the achievements of the doctrine of law regarding the legal status and basis for charging entrance fees to national parks and nature reserves, as well as to identify functions fulfilled

by such fees. A hypothesis according to which the aforementioned fees are a special type of public levies included in the category of environmental levies for the possibility of using public facilities was verified. The motive for their establishment is the legislator's intention to transfer onto natural persons part of costs generated in relation to the operation of special areas in the form of national parks and nature reserves. The study applied the dogmatic and legal method as dominant, and the empirical and analytical method as supplementary.

2 Principles for charging and collecting entrance fees to national parks

Equivalency of public levies is their relevant feature, i.e. the entity paying a fee receives consideration from a public law entity receiving the fee, yet not in all cases the amount of the paid fee corresponds to the value of this performance (Gliniecka, 2007: 13). The beneficiaries of proceeds from entrance fees to national parks are organizational units of the public finance sector, i.e. state natural persons referred to in Article 9 section 17 PFA. This category includes i.a. national parks, therefore fees for entry to national parks or for providing access to them may be considered a form of public levies. This statement is grounded in Article 5 section 2 subsection 1 PFA which stipulates that a fee is a public levy when the obligation to pay it for the benefit of public finance sector units results from a separate act (Ofiarski, 2013: 25). A different view is also formulated in the doctrine, according to which such fees are not a kind of a public levy and have the character of a price for entry onto somebody else's property (Lipiński, 2006: 159).

The equivalency attribute of the discussed fee means that the performance that the fee-payer may request is the right to enter a national park or its certain areas or a request for access to the national park or its certain areas. Pursuant to Article 5 section 22 NCA, providing access means allowing the national park or its certain areas and facilities to be used for scientific, educational, tourist, recreational and sporting purposes, for filming and photographing, as well as for profit. The scope of the performance involving entrance to a national park is narrower and pursuant to Article 5 section 26 NCA it includes walking or driving into an area covered by strict or active

protection, for scientific, educational, tourist or recreational purposes. Thus, the possibility of pursuing sporting and profit-generating purposes was excluded, and so was filming and photographing. Paying an entrance fee to a national park means that park visitors may also use its infrastructure, including walking trails modernized as part of the project (Director of the National Revenue Information: 0111-KDIB3-2.4012.576.2017.3.AR).

The legislator did not establish an ultimate obligation to charge the discussed fees since Article 12 section 3 NCA features a statement "fees may be charged". Introduction of these fees is determined by way of a decree (Decree of the Minister for the Environment of 18 March 2013) by a minister competent for environmental matters. On the basis of Article 12 section 10 NCA he was authorized to specify national parks and their certain areas where entrance fees are charged. When issuing a decree in this matter he should apply appropriate statutory guidelines, i.e. take into account the diversity of natural and landscape values of national parks, the volume of tourist traffic and its influence on the nature of national parks. The Decree of the Minister for the Environment provides that fees are charged for entrance to seven national parks (Biebrza, Bieszczady, Karkonosze, Magura, Narew, Tatra and Wigry), while as regards other national parks fees are charged only for entrance to its certain areas (these include the areas of the following parks: Babia Góra, Biała Wieża, Gorce, Bory Tucholskie, Polesie, Roztocze, Słowiński and Świętokrzyski). The list above shows that according to the legal status as of 31 December 2018 fees were not charged for entry to eight national parks: Drawa, Kampinos, Ojców, Stołowe Mountains, Warta Mouth, Pieniny, Wielkopolska and Wolin. It can be concluded that an entrance fee does not have a universal character in the material meaning and is a levy introduced *de facto* by the Minister for the Environment.

The Minister for the Environment only decides in which national parks or its areas an entrance fee shall be charged, while the price of the fee is determined, pursuant to Article 12 section 4 NCA, by the director of the national park who is its body appointed by the minister for the environment. If the director of a national park fails to determine a specific rate of the fee, charging it is not possible (Radecki, 2015: 24). The director's task is to manage the operation of the national park and represent the park.

The director of a national park does not have full discretion in determining the prices of fees since Article 12 section 5 stipulates for the maximum price of a fee for a single entry to the park. It cannot exceed the amount specified in the statute, valorized for the forecasted average annual total consumer price index, adopted in the Budget Act (in 2019 the maximum price is PLN 8). The fee is paid through purchasing a single entry ticket or a multiple entry ticket in fee collection points or by paying into the national park's bank account.

Article 12 section 7 NCA specifies the catalogue of entities exempt from the obligation to pay entrance fees to national parks. The list of exemptions is exhaustive therefore the statutory catalogue is of a closed nature. The national parks' directors' discretion to create further exemptions was not provided for either. The statutory catalogue of exemptions was constructed taking into account different criteria (status of a natural person or purpose for being in the area of the national park). Those exempt from the obligation to pay entrance fees to a national park include the following: children under the age of 7; persons holding a permission from the director of the national park to carry out scientific research in the scope of nature conservation, school goers and university students participating in classes taking place in the national park in the scope agreed with the director of the national park, residents of communes located within the borders of the national park and in communes bordering the national park, persons visiting designated beaches in the national park, persons visiting places of worship, members of a large family with a valid Large Family Card (Act on the Large Family Card, Article 4).

Moreover, the legislator introduced discounts for entrance fees to national parks at 50 % of the fee price determined by the director of the national park. The catalogue of discounts also has a closed nature and pursuant to Article 12 section 8 NCA includes school goers and university students, children and youth under the age of 18; pensioners; disabled persons; soldiers in active service.

The levy-imposing power includes only two areas related to the functioning of entrance fees to national parks. The first area concerns the Minister for the Environment's specifying these parks or parts thereof in which fees

shall be charged, whereas the second area involves determining the price of the fee by the director of a national park taking into account the restrictions adopted in the act (maximum fee price and the applicable catalogue of exemptions and discounts). It is estimated that through the introduction of statutory restrictions in shaping the price of entrance fees to national parks the citizens' right to universal access to public goods that include such parks is guaranteed (Zaborniak, 2017: 235).

Adopting such a concept that defines the scope of the power, however, means that different charges related to the discussed fees may be applied with regard to individual national parks (from complete resignation from these charges to adopting highest possible fees stipulated by the statute). Solutions applied in the Karkonoski National Park may serve as an example here, i.e. individual one-day tickets (PLN 8 for a full price ticket and PLN 4 for a discounted ticket), one-day tickets for groups participating in guided tours (PLN 7 for a full-price ticket and PLN 3,50 for a discounted ticket) and individual three-day tickets (PLN 20 for a full-price ticket and PLN 10 for a discounted ticket). Annual and single-entry charges for entry in a motor vehicle onto internal roads of the Karkonoski National park were also determined (Order of 30 August 2018), e.g. for one car with the total weight not exceeding 3.5 tons (PLN 1 500 annually or PLN 250 for a single entry) or for one snowmobile (PLN 1 000 annually or PLN 250 for a single entry). The following fees for tickets were established in the Biebrzański National Park (Order of 30 April 2018): one-day ticket (PLN 6 full-price and PLN 3 discounted); three-day weekend ticket (PLN 12 full-price and PLN 6 discounted); week ticket (PLN 30 full-price and PLN 15 discounted); two-week ticket (PLN 55 full-price and PLN 27.50 discounted); annual (PLN 100 full-price and PLN 50 discounted). Pursuant to Article 108 section 5 subsection 2 NCA Park Guard officers are authorized to inspect evidence of payment of entrance fees to the national park.

Proceeds from entrance fees to national parks are one of the sources of the parks' income. The catalogue of these sources, specified in Article 8h NCA, covers 15 types of permanent incomes and 8 types of incomes of an extraordinary nature (e.g. voluntary payments, inheritance, legacies and donations). Entrance fees to national parks were included in the category of permanent

incomes, which should be assessed critically in the light of the presented principles of their introduction and collection. They do not occur in all national parks established in Poland, but only in those which were indicated by the Minister for the Environment. The total sources of incomes of national parks may also be classified according to the criterion of discretion in using the proceeds coming from these sources. Certain incomes were tied by the legislator with specified tasks carried out by national parks (e.g budget allocations). Entrance fees to national parks fall in the second category of incomes, that is those not related to the obligation of spending on strictly defined tasks (Zbaraszewski, 2016: 363). The sums of proceeds from these fees vary between individual national parks, e.g. the highest annual proceeds are achieved in the Tatra National Park (approx. PLN 12 million a year), the Karkonoski National Park (approx. PLN 2,8 million a year) and the Bieszczady National Park (approx. 1,8 million a year). The lowest proceeds are recorded in the Polesie National Park (approx. PLN 70 000 a year) and the Narew National Park (approx. PLN 70 000 a year).

The normative concept of the fees in question is similar to the local fees applicable in Poland and in other countries, the implementation of which in a given area is decided by local governments. In Poland, these are i.a. local and health resort fees (taxes) introduced in areas that meet statutory requirements determining the possibility of staying there for tourist or health purposes. The introduction of local fees is also possible in other countries, and the inflows from the aforesaid fees supplement the financial resources of communes necessary for the proper implementation of public tasks (Tomášková, Mrkývka: 2018).

3 Entrance fees to the area of a nature reserve

The authority to introduce entrance fees to the area of a nature reserve is granted to the regional director for environmental protection who holds the legal status of a body in terms of nature conservation (Article 13 section 4 NCA). It is a monocratic body, acting within competences vested in it by law, located in the state's organizational structure, taking action on behalf and for the account of the state, authorized to use sovereign measures and appointed in order to implement norms of the nature conservation

law (Mierzejewski, 2006: 95). The legislator conditioned the introduction of fees for entrance to the area of a nature reserve by the need to protect nature.

The catalogue of sovereign measures afforded to the regional director for environmental protection with regard to nature reserves and applied by issuing an act of a local law in the form of an order includes:

- recognizing a given area as a nature reserve (the order specifies its name, location or course of its borderline and the reserve's lag, conservation objectives and the kind, type and sub-type of the nature reserve, as well as the entity supervising the reserve),
- increasing the area of the nature reserve, changing conservation objectives, and in case of irretrievable loss of natural values for which the reserve was established, reducing the area of the nature reserve or its liquidation,
- introduction of entrance fees to the nature reserve area.

It needs to be stressed that recognizing a given area as a nature reserve or its increase does not automatically create an obligation to introduce an entrance fee. There may be nature reserves where entrance will not entail an obligation to pay fees. Introducing such a fee is only a right afforded to the regional director for environmental protection, while the need for nature conservation is the premise justifying its introduction. Pursuant to Article 2 section 1 NCA nature conservation involves preserving, sustainable use and recreation of resources, formations and elements of nature: wild plants, animals and fungi; plants, animals and fungi under species protection; migratory animals; natural habitats; endangered habitats, rare and protected species of plants, animals and fungi; formations of living and inanimate nature as well as plant and animal fossils; landscape; greenery in urban and rural areas; forest cover. The occurrence of the need to protect any of the aforementioned goods may justify the recognition of a given area as a nature reserve, and subsequently the introduction of an entrance fee to such an area.

Pursuant to Article 5 section 26 NCA entry to a nature reserve means walking or driving into an area covered by strict or active protection, for scientific, educational, tourist or recreational purposes. The quoted provision shows that entry to a reserve was limited only to the achievement

of specifies purposes (scientific, educational, tourist or recreational) and to specified areas of protection (strict or active). This leads to a conclusion that in practice it is possible to stay in a reserve for purposes that are not indicated by law or in the area of protection, which does not fall under the entry to the reserve defined by the legislator, thus it will not be subject to a payment obligation, e.g. staying in the area of the reserve in order to carry out commercial or agricultural activities (Olejarczyk, 2018: 276).

In contrast to entrance fees to national parks, the legislator did not regulate any structural elements of entrance fees to nature reserves (the basis, discounts and exemptions, payment conditions) and limited himself only to specifying the maximum fee price. A single-entry fee to a reserve could not exceed PLN 8 in 2018. A statutory mechanism for valorization of this amount by the forecasted average annual consumer price index was introduced, adopted in the Budget Act. Adhering to the statutory price limit, the regional director for environmental protection establishes prices of entrance fees to nature reserves.

According to Article 13 section 6 NCA proceeds from these fees are allocated for nature conservation. However, the quoted provision does not indicate whether they should be used for such purposes in the nature reserve in which they were collected or in any other nature reserve. The interpretation problem is related to the lack of statutory regulation that would define both the beneficiary and the disposer of proceeds from fees charged. One can only postulate the supplementation of legal regulations concerning the categories of tasks the implementation of which can be financed under the general objective listed in the Act, which is nature conservation.

The taxation power characteristic of the authorities participating in setting admission fees to special areas and public law status of these fees and the allocation of cash inflows from such fees justify the postulate to clearly specify in the Nature Conservation Act that the provisions of the Tax Ordinance Act apply to these fees. It contains provisions common to all taxes and public fees, including the competences of tax authorities and other bodies that have the rights of tax authorities (Brzezicki, Morawski: 2016).

4 Conclusion

National parks and nature reserves are special areas created in order to protect various elements of nature. Carrying out an activity on their area is restricted or even prohibited, because the regulation's objective is preservation, sustainable use and restoration of nature's resources. Entrance fees to national parks and nature reserves are a legal and financial instrument used to implement this objective. Introducing these fees is not obligatory with regard to each national park or nature reserve. In the case of national parks, the decision on introducing a fee is made by the Minister for the Environment (he specifies national parks where entrance fees shall be charged by way of a decree) and the director of the national park who establishes the price of these fees. The decision on the introduction of entrance fees to a nature reserve is made by the regional director for environmental protection.

In the case of introducing admission fees into the area of a national park or nature reserve, they become obligatory fees in the sense that a person intending to use the right to enter such a special area is obliged to pay the appropriate fee. It can be stated that the fee is characterized by the value of equivalence, because its payment entitles you to enter the special area. The fees are also intentional, because inflows from these fees are allocated to the implementation of various public tasks in the field of environmental protection.

The research conducted in the study proves that despite modest statutory regulations regarding entrance fees to national parks and nature reserves, it can be assumed that they are of a public law nature. They are introduced by way of sovereign administrative acts in the form of a minister's decree or acts of local law (Wilk, 2015: 34). The decision on introducing them is made, within statutory boundaries, by public administration entities who are afforded the status of nature conservation bodies. These bodies carry out specified public tasks in terms of nature conservation, while whole proceeds from the discussed fees are one of the sources of financing such tasks. The cash sums collected from entrance fees to national parks and nature reserves are public sources in the meaning of the Public Finance Act.

However, it is possible to submit a postulate to the legislator for more detailed regulation of some structural elements of the discussed fees at the level of the Act. Assuming that this is a special form of public tribute, the standards formulated in art. 84 and art. 217 of the Constitution of the Republic of Poland of 2 April 1997 must be fully respected. According to these constitutional standards, public legal obligations and benefits, i.e. also fees, should be determined by law. The constitutional standard introduces the obligation to specify by law the entities obliged to pay public tributes, the subject of the fee and its rates, as well as the rules for granting allowances and redemptions and the category of entities exempt from fees.

Admission fees for national parks and nature reserves can be compared to some local (municipal) fees, in particular local and health resort fees. They do not have a general, i.e. nationwide nature in Poland. They can be introduced by municipal councils in areas that meet the criteria set by the legislator (climatic, landscape, health). The construction elements of such fees are specified in the Act, and the municipal council decides whether to enter them in a specific area and from persons temporarily staying in this area, setting the rates of fees that cannot be higher than rates adopted by law.

The fees presented in the study are not universal, because they are collected only in connection with access to some national parks and nature reserves. However, if a decision was made to introduce them, they can be classified in the category of fees charged for using public facilities, similar to road, harbour or airport charges (Klat-Wertelecka, 2013: 30). Persons paying entrance fees to national parks and nature reserves co-finance operating costs of these public facilities.

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Exemption of Port Infrastructure from Property Tax in Poland

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Abstract

The study presents, on the basis of an analysis of tax legislation, the case law and the achievements of the tax law doctrine, premises of and principles for exempting port infrastructure from property tax in Poland. Two divergent concepts have been identified. According to the first one, the exemption has a material and personal character and may be applied only when the port manager provides port services with the use of port infrastructure facilities. The second concept assumes solely the material character of the tax exemption, therefore it is applied not only in the case of providing access to port infrastructure facilities by the port manager, but also by any other entity that has this infrastructure to their disposal based on an agreement executed with the port manager. The second concept is more substantiated due to the purpose of port infrastructure facilities referred to in the provisions of the tax law act and due to the general nature of the statutory catalogue of tax exemptions. They are material exemptions, and thus established taking into account the way the object of tax is used and not due to the legal status of its holders, including a dependent possessor. In order to remove the current interpretation doubts concerning the nature and limits of this tax exemption it was suggested that the tax law act provision should be clarified by inserting into it a statement about the application of the exemption irrespective of whether the port infrastructure facilities are used directly by the body managing the port or by another dependent possessor, based on an agreement executed with the port's manager. The dogmatic and legal method was applied in the study as dominant, and the empirical and analytical method as supplementary.

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1 Introduction

The property tax applicable in Poland, regulated in the Act of 12 January 1991 on local taxes and fees (hereinafter: LTFA), does not have a character of a universally applicable public levy. This results from a comprehensive catalogue of personal and material exemptions from taxation. Among them, a material exemption regulated in Article 7 section 1 subsection 2 LTFA concerning port infrastructure facilities and infrastructure facilities providing assess to sea ports and harbours and land occupied by them is essential. The problem regarding the scope of taxation of real estate located in the areas of ports and marinas has been of interest to representatives of the Polish tax law doctrine for many years. The situation in this area is subject to dynamic changes due to frequent amendments to tax legislation and inconsistent court jurisdiction (Dowgier, 2012; Rolewicz, Szubert, 2012; Reiwer-Kaliszewska, 2018; Wróblewska, 2018).

Sea ports and harbours are an important component of the economy of any country. On the area of sea ports and harbours mainly traditional port services are performed (transport, transshipment, storage). New types of services are also carried out today, which are an effect of technical and technological progress (Adamowicz, 2017: 3). Proper operation of sea ports and harbours requires high investment outlays and renovation expenses (Grzelakowski, 2015). Application of exemptions from taxing port property is a form of support that the state provides to bodies responsible for an adequate technical state of port infrastructure facilities. Tax payers exempt from the obligation to pay tax have greater capacity to invest in port infrastructure and to bear the costs of its day-to-day operation and renovation. The local taxes and fees act does not define the terms "facilities", "port infrastructure" or "infrastructure providing access to sea ports and harbours". Therefore, the aim of this study is to show the need to use the systemic interpretation when setting limits of this tax exemption. Only a joint application of the act on local taxes and fees and the Act of 20 December 1996 on sea ports and

harbours (hereinafter: SPHA) and the Act of 7 July 1994 Construction law (CLA) results in an appropriate application of the tax exemption to facilities forming port infrastructure.

The hypothesis that an appropriate amendment of the content of the provision of Article 7 section 1 subsection 2 LTFA could result in removal of interpretation doubts about retaining the right to exempt port infrastructure facilities and infrastructure facilities providing access to sea ports and harbours from taxation was subject to verification. One can suggest in this scope adding a statement to this provision stipulating that the tax exemption is applied irrespective of whether the facilities making up this infrastructure are at the disposal of the body managing the sea port (harbour) or whether this body has given them over to another person as a dependent possessor, e.g. to a lessee. The tax exemption regulated in Article 7 section 1 subsection 2 LFTA has a material character (Wołowiec, 2014: 31), not a personal or a mixed one, that is material and personal. The application of the tax exemption is determined by the purpose of these facilities regardless of whether they are at the disposal of the body managing the port or another entity based on an agreement executed with the body managing the port. In turn, the case law, divergent in this respect, proves that in practice there are problems related to the appropriate application of provisions regulating the discussed tax exemption. In view of the above an amendment specifying the essence of this exemption as a typical material exemption is necessary. Bearing in mind the purpose of this study and the adopted hypothesis, the tax legislation as well as the case-law and the achievements of the doctrine of law that concern this tax exemption were examined and evaluated. The dogmatic and legal method was applied is the study as dominant, and the empirical and analytical method as supplementary.

2 The object of the tax exemption

The legal structure of the tax exemption in question allows distinguishing in it three objects exempt from property tax, that is "port infrastructure facilities", "infrastructure facilities providing access to sea ports and harbours" and "land occupied by such facilities" (Kopyściańska, 2015: 329). This means that land not occupied by facilities of the aforementioned infrastructure

cannot be exempt from property tax even if it is located in the port area or if it provides access to the sea port or harbour. For this reason, it can be assumed that land that has not been occupied by the facilities of the infrastructure in question is not an independent object of the tax emption because it features jointly with the facilities located on it in the structure of this exemption.

According to Article 3 section 3 CLA a facility encompasses any construction work that is not a small architecture building or facility, that is: a linear facility, an airport, a bridge, a viaduct, a flyover, a tunnel, a culvert, technical networks, free-standing antenna masts, free-standing advertising boards and advertising devices permanently bound with the ground, earthworks, defence structures (fortifications), shelter structures, hydrotechnical structures, containers, free-standing industrial installations and technical devices, sewage treatment plants, landfills, water treatment stations, retaining structures, overground and underground pedestrian crossings, utility infrastructure networks, sports buildings, cemeteries, monuments, as well as construction parts of technical devices (boilers, industrial furnaces, power plants, wind farms and other devices) and foundations for machinery and equipment as separate, in technical terms, components of objects forming the usable whole.

Facilities have a more diverse nature than buildings and frequently a few construction works remain in a functional relationship. In this case, one construction work is formed by a few structures forming the technical and usable whole, that is connected in such a way so that they are suitable for specific use according to technological requirements. One cannot exclude here that each of these elements can be an independent object, though it may not always be used independently for a specific purpose (II FSK 1979/16).

Not all of the above mentioned facilities, due to their purpose, may form part of the port infrastructure or infrastructure providing access to sea ports and harbours. According to Article 2 section 4 SPHA, port infrastructure means port waters and generally available facilities, devices and installations, located within the boundaries of the sea port or harbour, related to the port's operation, intended for the port managing body's provision of services related to the use of this infrastructure. According to Article 2 section 5 SPHA

the term "infrastructure providing access to sea ports or harbours" means fairways leading to the sea port or harbour, located within the boundaries of the sea port or harbour, together with the facilities, devices and installations related to their operation. The following facilities, among others, from the extensive catalogue of structures listed in Article 3 section 3 CLA should not be classified in the statutory category of "port infrastructure" or "infrastructure providing access to sea ports or harbours": free-standing advertising boards and advertising devices permanently bound with the ground, cemeteries, monuments, fortifications, sports facilities. Excluding them from these categories is determined by such premises as no connection to the port's operation or an absence of a necessary provision of access to the port. Port infrastructure must most of all include industrial installations, technical devices, containers, linear facilities (e.g. roads, railway lines together with sidings (decision of the Appellate Court: ACa 83/17)), pipelines, gas pipelines, above-ground cable lines, container terminals (I SA/Gd 885/12).

The tax exemption, regulated in Article 7 section 1 subsection 2 LTFA, concerns only the infrastructure located in sea ports or leading to sea ports and harbours. However, it does not include other ports and harbours, e.g. river or inland ones. When interpreting Article 7 section 1 subsection 2 LTFA it is justified to apply non-linguistic methods, i.e. systemic or historical interpretation, related to the mode in which this provision was introduced into the act on local taxes and fees. Therefore the term port infrastructure on the basis of this tax law needs to be associated solely with a sea port, not a river or inland port (I SA/Bd 638/14). This tax exemption does not have a universal nature as it does not cover infrastructure in all types of ports (II FSK 1222/12). This means that infrastructure located on the territory of inland or river ports and harbours is subject to taxation (Pahl, 2012: 18–19). However, a different view may be invoked, according to which the exemption laid down in Article 7 section 1 subsection 2 LTFA also includes port infrastructure in river ports (Zarzycka-Ciołkiewicz, 2014: 194). As a consequence of adopting this view, a different material scope of the tax exemption in question would be applied on the basis of Article 7 section 1 subsection 2 LTFA. With regard to port infrastructure, it would include all facilities

of this infrastructure, regardless of whether they are located in a sea port or a river port, whereas exemption of infrastructure providing access to the port would apply exclusively to facilities providing access only to sea ports and harbours. However, such an internal division of the tax exemption is not justified since the adjective "sea" applied in the content of Article 7 section 1 subsection 2 LTFA should be used in reference to all phrases following it, i.e. "port infrastructure" and "infrastructure providing access to ports and harbours".

The literature also formulates an extremely different view, according to which due to the absence of a legal definition of the term "port infrastructure" in the act on local taxes and fees, its interpretation should be performed according to linguistic rules, and thus referring to its meaning in common language and omitting the rules of systemic interpretation, including the definition of "port infrastructure" adopted in the act on sea ports and harbours. Assuming the primacy of the linguistic interpretation over other interpretations, it was concluded that it is not appropriate to use a different type of interpretation where the linguistic interpretation brings sufficient results (Dembiński, 2015: 33).

2.1 The scope of the tax exemption of port infrastructure facilities in the achievements of the case-law and in the doctrine of the tax law

On the basis of an analysis of the achievements of the case-law formed since the introduction to the tax law of the provision of Article 7 section 1 subsection 2 LTFA, i.e. since 1 January 2002, one can distinguish two main case-law lines concerning the exemption from tax of port infrastructure facilities and facilities of the infrastructure providing access to sea ports and harbours and land occupied by them. According to the first concept, this exemption should be treated as an exemption of a material and personal character, and thus is afforded only to the port manager who uses this infrastructure to perform various port services. The second concept assumes that this exemption is only a material exemption, i.e. referring directly to the infrastructure facilities, and thus is afforded regardless of whether they are used directly by the body managing the port or by another entity subsidiary

to it on the basis of e.g. a lease agreement (with or without the right to collect fruits). Both concepts occur in parallel and neither of them has become dominant. A similar polarization of positions is noticeable in the doctrine of the tax law. It is not a favourable phenomenon for entities providing port services using such infrastructure, because case-law and doctrinal discrepancies cause a sense of non-stability in terms of the scope of tax obligations relating to this infrastructure.

Appellate courts, emphasizing the mixed, i.e. material and personal, character of the discussed tax exemption invoked various arguments that were supposed to substantiate this concept. It was pointed out that the tax exemption includes only the infrastructure which is intended for the managing body's performance of tasks in terms of provision of services related to the use of it, as only such infrastructure has the attribute of port infrastructure. Giving devices and facilities the status of "port infrastructure" was associated with their purpose of performing tasks in terms of provision of services related to its use by the managing body. Not any entity can be this body, but only an entity which was established in a way prescribed by the legislator in the sea ports and harbours act (I SA/Gd 321/18). Therefore, the tax exemption can be enjoyed only by the body managing the port (II FSK 1229/14). The material aspect of the exemption results from the fact that it concerns objects of taxation falling under the category of port structures and land, whereas the personal aspect is manifested in the fact that the entity providing services by means of these facilities and on this land (the entity using these facilities and land) must be the entity managing the port (I SA/Gd 989/13). The courts justify the adoption of such an interpretation of Article 7 section 1 subsection 2 LTFA by the nature of this provision. It is a special provision establishing an exception from the principle of universality of property tax, and thus it should be interpreted by applying a strict linear interpretation (II FSK 1230/14). It is concluded that the legislator's intention was exclusively to grant tax preferences to bodies managing sea ports (II FSK 1222/12). Summing up this case-law theme, one can assess that courts do not limit the interpretation solely to the content of the provision of Article 7 section 1 subsection 2 LTFA, but also take into account the content of Article 2 subsection 4 and

Article 7 section 1 subsection 5 SPHA. The listed provisions jointly create a legal norm that introduces the tax exemption. As a consequence the courts conclude that this tax exemption refers directly to the bodies managing a sea port (I SA/Gd 223/14). Such a way of interpreting the above-mentioned provisions is accepted in the doctrine, but not without specified reservations. It is concluded that one can characterize the discussed tax exemption as material and personal, thus addressed to the bodies managing ports and using the facilities of port infrastructure with the purpose of providing port services. The theory's inconsistency with practice is pointed out since often the body managing the port does not provide port services independently, but through other entities. As a consequence, the port infrastructure facilities together with land cannot enjoy the exemption from property tax (Dowgier, 2012: 42).

Adopting the second concept according to which the tax exemption has only a material character and is associated with the essence and functions fulfilled by the port infrastructure or the infrastructure providing access to sea port and harbours, administrative courts support this view with the following arguments. Giving the port infrastructure over by the body managing the port to another person as a dependent possessor does not eliminate rights to enjoy the tax exemption (I SA/Sz 164/17). The port manager leasing (with the right to collect fruits) a specified part of the port infrastructure to another entity does not prejudge the change in its use in a situation where this other entity makes it available in accordance with its purpose (I SA/Sz 84/17). The provision of services related to the use of port infrastructure involves it performing an administrative and coordinating function, and also providing port users with access to the port infrastructure through leasing it (with or without the right to collect fruits). Leasing (with or without the right to collect fruits) of the port infrastructure facilities to port operators by the port managing body is irrelevant to meeting the requirements of the tax exemption (I SA/Sz 40/17).

Concluding that the tax exemption has solely a material character, the need to differentiate between the statement "provision of services related to the use of port infrastructure" and the term "activity in the sphere of operation conducted within the boundaries of sea ports and harbours", carried

out by companies acting in the sphere of operation, and thus entities managing the port infrastructure who are not bodies managing the port, was pointed out. Operational activity cannot be carried out by entities managing sea ports of key importance for the national economy (ports in Gdynia, Gdańsk, Szczecin and Świnoujście). Therefore, leasing (with or without the right to collect fruits) of the port infrastructure does not lead to restricting or excluding the universal accessibility of port infrastructure referred to in Article 2 subsection 4 SPHA. The general accessibility is provided for by administrative law provisions which also apply to entities managing port infrastructure, and their validity cannot be excluded by civil law agreements (I SA/Gd 1411/13). The essence of the property tax exemption is whether such property is used by this entity to perform tasks specified in the act on sea ports and harbours and not who owns it (I SA/Gd 961/12).

The analysis of courts' decisions, which assume that the tax exemption specified in Article 7 section 1 subsection 2 LTFA has a solely material character, shows that using the definition of "port infrastructure" from the act on sea ports and harbours does not change the material nature of this exemption. The tax law does not require the tax payer to be the body managing the port. It is essential that the port infrastructure components serve the performance of tasks of the body managing the port. Therefore, if the body managing the port gives the port facilities, devices and installations over to other entities for usufruct, lease (with or without the right to collect fruits) or on the basis of another agreement, these facilities held by the entities other than those managing the port also enjoy the tax exemption (I SA/Sz 402/07).

The view according to which the fact of leasing (with or without the right to collect fruits) or giving the port infrastructure over for paid use to entities other that the body managing the port cannot cause the loss of the right to the tax exemption is right. Adopting a different assumption would lead to a situation where the tax exemption could not be enjoyed by any entity, i.e. neither the body managing the port nor the entity providing services using the port infrastructure. Such an interpretation of statutory provisions would be contrary to their *ratio legis*, as the tax exemption would be an empty regulation. Adopting a different interpretation, thus one upholding the property tax exemption for bodies managing ports, despite their leasing

(with or without the right to collect fruits) of the port infrastructure, leads to an increase of their financial capabilities (stimulating activity) in order to perform statutory tasks, and thus primarily in order to build, expand, maintain and modernize this infrastructure and also to acquire land for the needs of the port's development. Moreover, a different interpretation would lead to cancelling the lease resulting in a decrease of proceeds to the bodies managing the ports and would also limit the capabilities of the managing bodies in terms of maintaining and modernizing this infrastructure (Aromiński, 2013: 31). Another entity using the leased port infrastructure also performs port services related to it. It does not change its primary purpose which is a fundamental requirement of the material exemption from property tax (Wołowiec, 2018: 77). A similar stand is taken by other authors who emphasize that the property tax exemption involves all port infrastructure facilities and land occupied by it, regardless of the status of the entity who is the payer of this tax. At the same time they point out that the provisions of the act of sea ports and harbours do not provide that the entity managing the port is obliged to perform the tasks involving the provision of port services using this infrastructure directly and independently. The tax exemption should also be applied when such tasks are carried out by another entity on the basis of an appropriate agreement with the body managing the port. It is also emphasized that the so called third parties may cooperate with those managing the ports under different terms (Rolewicz, 2012: 33), and therefore formulating a thesis about a material and personal nature of the tax exemption established in Article 7 section 1 subsection 2 LTFA is considered unsubstantiated (Zarzycka-Ciołkiewicz, 2013: 19).

3 Conclusion

The analysis and assessment of the achievements of the case law and the doctrine of the tax law carried out in the study showed that two different concepts have formed concerning the character and scope of exempting "port infrastructure facilities" and "port infrastructure facilities providing access to sea ports and harbours" from tax. According to the first concept, the tax exemption had a material and personal character and in order for it to be applied it is not only necessary to correctly classify specified facilities

to the notional category "port infrastructure" but also to make it available directly by the body managing the port. Such requirements are justified by a catalogue of statutory tasks where the obligation of performing them is addressed to the port manager, including primarily the provision of services related to the use of port infrastructure. Where there in an approval for such understanding of the status of the tax exemption it is concluded that the port managing body's giving the port infrastructure and land related to it over for lease (with or without the right to collect fruit) or on the basis of a different agreement for paid use of the port infrastructure results in the managing body's loss of the exemption from property tax. However, it needs to be noted that such results do not encumber infrastructure facilities providing access to sea ports and harbours, even if they are located within the boundaries of the sea port or harbour.

The second concept identified in the case law and the doctrine assumes that the discussed tax exemption has an exclusively material character. The tax exemption concerns port infrastructure facilities and infrastructure facilities providing access to sea ports and harbours due to their purpose and irrespective of whether they are administered by the body managing the port or another entity on the basis of an agreement executed with the body managing the port. Adopting this concept is substantiated primarily by placing the discussed tax exemption in the catalogue formulated in Article 7 section 1 LTFA which has a material character (it includes 19 types of exemptions in total). The status of these exemptions is clearly stipulated in Article 7 section 3 LTFA, according to which a commune council, by way of a resolution, may introduce material exemptions other than those specified in Article 7 section 1 LTFA, and therefore, this provision regulates material exemptions, not material and personal exemptions.

Opting exclusively for the material scope of the tax exemption regulated in Article 7 section 1 subsection 2 LTFA additionally allows treating in the same way all objects of exemption listed in this provision. With regard to infrastructure facilities providing access to sea ports and harbours, both those located on the area of ports or harbours and those outside their boundaries, it is not required that they should be made available directly by the body managing the port or harbour. The possible negation of the exclusively

material character of exempting "port infrastructure facilities" from tax may lead to an unsubstantiated division of the provision of Article 7 section 1 subsection 2 LTFA into two different parts. With regard to port infrastructure the tax exemption would have a material and personal nature, whereas in the case of infrastructure providing access to sea ports and harbours exclusively the status of a material exemption.

The need to carry out a systemic interpretation, resulting from the absence in the tax law of legal definitions of concepts constituting the construction of the tax exemption of port infrastructure facilities and infrastructure providing access to sea ports and harbours, should not result in the change of the legal character of this exemption from a material one to material and personal. The legislator's intention was to exempt from tax specified things (objects, assets), used for statutorily specified purposes. The application of definitions of concepts such as "facility", "port infrastructure" and "infrastructure providing access to sea port and harbours", formulated in the provisions of construction law and the act on sea ports and harbours, is necessary to set material boundaries of the exemption from property tax which is a wealth (*in rem*) tax, and not a personal tax. Essential interpretation doubts, which lead to a discrepancy in courts decisions and polarize views of doctrine representatives, confirm the hypothesis of the need to amend Article 7 section 1 subsection 2 LTFA. Removal of such doubts is possible by including a reservation in the content of this provision which would state that the tax exemption is applied irrespective of whether the port infrastructure facilities are used directly by the body managing the port or by another dependent possessor, on the basis of an agreement executed with the port manager.

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Issues Related to Wind Power Plants Taxation. A Comparative Analysis Based on French Tax Law Regulations

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Abstract

The general purpose of the article is to present how the regulations related to wind power plant taxation may be composed. In some countries, over the past several years, the legislature has modified the regulations many times and introduced a lot of instability in this field. This may be one of the factors responsible for discouraging the investors from placing their assents into wind power plants industry. As some legislators seems not to have a clear vision of a coherent and permanent legal framework in this aspect, the present article describes the principles of taxation of wind power plants in one of the major EU economies – France. In the authors opinion the experience of French legislator in this regard may be helpful in creating a model of taxation of wind power plants not only in Poland but also in other East and Center European Union Countries**.**

Keywords: Tax Law; Wind Power Plant; French Law; Comparative Law.

JEL Classification: K34; K32.

1 Introduction

A growing interest in renewable energy sources in all EU member states is a fact. This is primarily related to the way of development that was chosen in the World as a response for the issues resulting from the global warming process (McKenzie, 2008: 679). Investments in renewable energy sources

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require considerable funding and their rate of return is relatively low. Aside from expenditures related to implementation of such investments, energy companies must from the beginning take into account possible tax burdens involving assets used for this purpose. In the Polish legal system, of key importance is the property tax. Unfortunately, in recent years, the Polish tax legislation regarding facilities and structures used for wind power plants has been changed several times. Undoubtedly, this whole situation can not convince the operators to invest in the assets that generates power from renewable sources and creates a legal uncertainty for wind power plants investments (Fabrizio, 2013: 765).

The lack of stable tax legislation may prove to be one of the main reasons for discouraging economic operators from pursuing such investments. The constant changes in the regulations regarding taxation of wind power plants seem absolutely incomprehensible. It is worth to underline that the recent amendments introduced to the laws and regulations which provide for imposing a property tax on wind power plants can be used as an academic example of how not to make tax law. In Poland, over the past several years, it has become a disgraceful standard to amend the legislation on local taxes when adopting other laws.

The situation related to legal framework of wind power plants in Poland was an impulse for the authors to start a comparative research in this field. Namely the authors wanted to analyse the taxation model of wind power plants in other EU countries. Perhaps the wider experience of France in this regard will help to develop a model of taxation of wind power plants in Poland that would be a solution for instable and frequently changed regulations. The purpose of this article is to present how the principles of taxation of wind power plants in France have evolved and compare them to the recent changes in this field that were made in the polish legal system.

2 Taxation of wind power plants in France

2.1 Introduction

Regarding the problems related to wind power plant taxation, the authors considers as very interesting to describe the experience of the French

legislator in this field. As it was already supposed, French experience in this regard may be helpful to develop a model of taxation of wind power plants not only in Poland but also in other East and Centre European Union Countries.

Renewable energy sources occupy a very important place in the French economy. This can be proved by the fact that the French government has already launched in 2008 the program of financial support for technologies related to renewable energy and biofuels. The value of the program was estimated at 1,35 billion EUR. The program included 450 million EUR in subsidies and 900 million EUR in loans. France is one of the first countries where a "friendly policy" has been adopted for pro-ecological investments (Geitmann, 2007: 10).

Nevertheless, apart from the traditional description and analysis of the nature of renewable energy sources in France, attention is drawn primarily to the fundamental obstacle to the development of renewable energy in this country, which is nuclear energy. France, in the light of many reports, has the potential of renewable energy sources, that is not fully used. However, in the case of France, the use of its renewable energy potential will not be easy, as nuclear energy exchange is a long and complex process. Indeed, the cost of replacing nuclear energy by the renewable one would be too burdensome for consumers, businesses, central and local government. The transition from nuclear energy should be made gradually and in stages, that leads to the conclusion that France needs long decades to fully use its potential of renewable energy sources. For this reason, however, legal changes in the field of renewable energy take place in an evolutionary manner and are characterized by high legal stability in this area.

3 Wind energy development in France

In the field of wind energy, France is characterized by quite a large geographical diversity. There are regions specializing in wind energy production, the most concentrated in the Center (244 MW), Languedoc-Roussillon (215 MW) and in Brittany (169 MW). In parallel, there are also regions that do not produce wind power at all: Alsace, Burgundy and Aquitaine. Wind

energy production (énergie eolienne) has been growing steadily in France since 2000. In fact, between 2003 and 2005, wind power production increased by more than 62 %. Between 2007 and 2009, by almost 50 % (Source Raport INSEE, 2008: 17).

The leader of wind energy in France is EDF Energies Nouvelles (in 50 % related to the EDF Group). EDF Energy obtained the ISO 14001 certificate for its activities in the wind energy industry. France is also the second European country in terms of the number of wind power plants just after Great Britain. At the same time, it is a country where these resources belong to the least exploited. The French coasts (Brittany and the Mediterranean), despite being exposed to very strong winds, are very poorly equipped with wind farms. The Atlantic coasts and the central regions of France are the regions with very low wind rates, which explains the almost complete lack of wind farms in these areas. France is aware of its potential in the field of wind. However, the EDF group increased significantly the capacity of wind installations from 1,300 MW (2005) to 14,000 MW (2010) and created an example of a model wind farm is the installation built in the village of Lévézou. This wind farm created by IRIS-Energy France, this largest farm in France with a capacity of 39 megawatts, consists of twenty six turbines of 1,5 MW each, whose construction cost amounted to 52,6 million EUR. This farm is able to supply energy to a city with around 134,000 inhabitants. As emphasized by specialists in the future, there will probably more attention to the construction of offshore wind farms, i.e. built at sea, away from homes (Vernier, 2005: 17). The capacity of these wind turbines at sea, in fact, will be 20–30 % higher than traditional land turbines. Forty of these marine turbines should be enough to produce enough energy to satisfy a city inhabited by one million inhabitants and numbering almost 400 000 households[3].

3 Therefore, in France, about 1 800 of these offshore wind turbines should satisfy 15 % of the energy demand, i.e. the equivalent of the energy generated by hydropower plants every year.

4 Challenges of the French energy industry

Currently, many studies indicate that the main obstacle to the development of renewable energy in France is not lack of funds or bad political will, but very well developed nuclear energy. It is emphasized that the development of renewable energy sources in France can only take place at the expense of nuclear energy, which is not an easy and not always economically viable process (Michon, 2010: 12). Is this "nuclear infatuation" not a burden in the long term that is hampering the development of modern, environmentally friendly energy in France?

Currently, France is the largest producer and advocate of the development of nuclear energy in Europe. In 2004, this country consumed almost half of the nuclear fuel in the EU, and the amount was almost three times higher than in Germany or Russia, i.e. countries taking up subsequent positions in this respect. At the EU summit in March 2007, France, together with Slovakia, Bulgaria and the Czech Republic, strongly supported the nuclear option as a way of moving away from fossil fuels. In France, as a result of the nationwide debate in 2003, it was stated that nuclear energy should remain one of the basic sources of energy. It is worth noting that France did not follow many European countries that have slowed down their nuclear programs after the Chernobyl accident in 1986. Thanks to this, electricity prices in France are one of the lowest in Western Europe[4].

It is worth to underline that in France, capital expenditures for the construction of a nuclear unit are among one of the lowest in the world. The country, wanting to become independent from the import of fuel, including nuclear fuel, launched a process of uranium enrichment as well as production of finished fuel. France is one of the few countries in the world engaged in the processing of spent fuel (Terneyre, 2009: 30). The acceptance of nuclear energy by the French society is expressed by the fact that large population centers were developed around nuclear power plants. For example, around 80 000 inhabitants live in a radius of 10 km from the Cattenom and Marcoule power plants. In addition, the nuclear industry in France

4 Only in 1977–1990, France built and commissioned 34 blocks with a capacity of 900 MW and 20 blocks of 1,300 MW, which gives an average of 4 large blocks per year.

gives employment of over 100 000 employees in the construction, operation, maintenance of nuclear power plants, fuel production and processing as well as waste storage. Nuclear reactors are an important export product of France. Nevertheless, in 2020 a large part of the French power plants will have to be either closed or modernized in order to be able to continue producing energy there (Terneyre, 2009: 30). This means that after 2020 a rather large development prospect for renewable energy opens up, including in particular for wind energy plants.

5 Taxation of wind energy

Power stations and wind parks (fr. parcs éoliens) are often classified as industrial units in France (fr. établissement industriels). An industrial entity, very often of a public nature, is a very broad concept referring to a legal person whose activity is financed partly from public funds to carry out missions in the field of broadly understood public interest (Braibant, Stirn, 2005: 127). A special kind of public units are the so-called public enterprises (fr. entreprise public), which are already legal entities governed by private law, but still financed from public funds aimed to meet the needs of communities and related to the public interest (Byjoch, Klimek, 2015: 12–13)[5]. In contrast to central administration bodies, public entities have far-reaching financial autonomy and administrative independence. The French doctrine (Serrand, 2012: 334–335) distinguishes two basic types of this institution: public administrative institutions (EPAs)[6] and public industrial and commercial enterprises (EPICs)[7]. The basic difference between the above-mentioned forms of public units boils down to the fact that industrial and commercial enterprises (EPIC) employ workers in principle under private law are subject to the rules applicable to private accounting and are not obliged to follow the law of public procurement in the selection of subcontractors and co-workers.

5 Sometimes in Polish literature a slightly different division can be found that enterprises publics fully operate on a commercial basis, while établissements publics does not.
6 Les établissements publics à caractère administratif (EPA).
7 Les établissements publics à caractère industriel et commercial (EPIC).

The taxation of entities producing wind energy is multifaceted, as four different taxes are included in taxation. A characteristic feature, however, is that in 70 % of these burdens are transferred to the communes' account, 27 % to the account of departments and only 3 % to the account of regions.

The basic tax for wind power plants is IFER – Imposition forfaitaire sur les entreprises de réseau. This tax is about 2/3 of the fiscal burdens that wind power plants have to face. In 30 % this tax goes to the departments, and in the remaining part to the municipalities or communes in which the wind farm was installed. Due to the above, this tax is very often in colloquial language assimilated to the expression wind tax (fr.taxe éolienne). According to Article 1519 D of the General Tax Code (CGI- code général des impôts), IFER is subject to land installations for the production of electricity using wind energy by mechanical means. The annual rate of this flat-rate tax is 7,47 € (in 2018) for each kilowatt of energy installed on 1 of January of the tax year[8]. It needs to be emphasized that from the above tax are excluded the installations whose capacity does not exceed 100 kilowatts.

It is only in the second place in the field of taxation of power plants and wind farms that we can find two real estate taxes, which is quite surprising due to the fact that they are the main and only form of taxation in Poland. Firstly, it is a classic tax on built-up properties (Taxe foncière sur les propriétés bâties (TFPB)) and a fee referring to the rent value of a property (CFE – Cotisation foncière des enterprises).

The developed property tax (TFPB) is determined on the basis of the value of the taxable rent (fr. valeur locative des biens imposables). The tax base is, therefore, the cadastral (rent) value being the equivalent of the hypothetical income from the real estate rented under normal market conditions (Etel, 2003: 30–31). This tax in accordance with the principle expressed in art. 1399 of the General Tax Code is payable to the commune where the property is located[9]. Property subject to taxation consists of objects attached to the floor and considered as "perpetual". These are the foundations, platforms,

8 Thus, an installed 3 MW wind turbine will generate a tax burden of 22 410 € (3000 kilowatts x 7,47 = 22 410).

9 Article 1399 CGI – Toute propriété foncière, bâtie ou non bâtie, doit être imposée dans la commune où elle est située.

delivery station and paths. Because the mast is a completely demountable and transportable metal structure, it is not an element subject to taxation. The property tax is due from 1 January of the year when the building was completed. New constructions are exempt from property tax, counting from the end of the year of their completion, during two consecutive calendar years. The exemption applies only to tax elements due to departments and regions, while the common part is never exempt (Article 1383 CGI). All contributions paid by the company are limited to 3 % of the value added of the investment.

In the case of the CFE tax, which is a part of the territorial company tax (CTE – Cotisation Territoriale des Entreprises), the tax base is also determined on the basis of the value of the taxable rent (fr.valeur locative des biens imposables). The taxable element of a wind power plant consists of fixed elements permanently attached to the ground (foundations, platforms, delivery station, road). Because the mast is a completely disassembleable and transportable metal structure (fr. entièrement démontable et transportable), this is not an element subject to taxation. As wind turbines companies have very often the legal form of previously described in the work établissements industries, they benefit from a 30-percent reduction in the calculation of their rental value. In addition, it is also possible to reduce taxation by 50 % in the case of equipment for the production of energy from renewable sources. The obligation to pay the CFE arises with the connection of the energy production installation to the network. Article 1465A of the General Tax Code also provides for a five-year tax exemption for companies which in particular create or develop industrial activities in the rural regeneration zones (ZRR – Zones de Revitalisation Rurale).

The last fiscal burden affecting wind power plants in France is a fee referring to the value added of enterprises – the so-called CVAE (Cotisation sur la valeur ajoutée des enterprises). Like the previous fee, it is part of the territorial tax on companies (CTE – Cotisation Territoriale des Entreprises). The proceeds from this tribute are distributed at a fixed annual rate. In 2018, the revenues of CVAE were allocated in 50 % to the region, in 23,5 % to the department and in 26,5 % to the municipalities or communes. CVAE covers

all companies subject to the previously described CFE, whose annual turnover exceeds 152 500 €. It is calculated at the close of the annual financial statements. The reference period is therefore the same as the tax year. The amount due for the fee is calculated on the basis of the value-added produced, that is, on the basis of operational revenue reduced by the operating costs. CAVE value is progressive and ranges from 0 % (companies whose turnover does not exceed 152 500 €) to 1,5 % for enterprises with a turnover of over 50 million €. Article 1465A of the General Tax Code (CGI – code général des impôts) also provides for a 5-year exemption for companies that carry out individual projects and extend industrial activities in the rural regeneration zones (ZRR – Zones de Revitalisation Rurale).

The French system seems to be more stable that the system in Poland, but it appears to be quite complex and not easy to understand for the international investor potentially interested in wind power plant installation development. That is why very often is underlined that the complexity of tax regulations is one of the biggest challenges for the local and public finances in France (Mariański, 2018: 89).

6 Taxation of power plants in Poland – the unstable and unconstitutional tax law

In the recent years, there has been a considerable interest in obtaining energy from renewable sources. But investments in renewable energy sources require a significant financial expenses and the rate of their return is relatively low. In addition to expenses related to the erection of this type of investments, energy entrepreneurs already take into account potential tax burdens on the assets used for this purpose at the stage of their planning. The Polish legal system gives to the property tax a key importance in this field. The problem is that in recent years the provisions of Polish tax law regarding the taxation of objects used to obtain electricity from wind energy (wind power plants) are unstable, like a flag in the wind. Undoubtedly, this situation is not an incentive to invest in assets used to obtain energy from renewable sources. Introduced legal regulations show the lack of the legislator's concept to create a model for taxation of wind power plants. However, it is true that some group of investors will employ a more intuitive and

less analytic approach in making their decisions, but most of them will try to analyse and compare the legal framework in at least two EU countries (Gilad, Kliger, 2008: 567). That is why the description of the French model in the previous chapters may be an interesting indication for the polish legislator. It is worth to underline that unstable tax law undermines both property interests of taxpayers and municipalities.

It is worth reminding that according to art. 16 point 2 of the Constitution of the Republic of Poland (Act of 2 April 1997, Journal of Laws Nr 78 pos. 483 as ammended) territorial self-government units participate in the exercise of public authority. It is not possible to "exercise" this power without adequate financial resources. For these reasons, in subsequent provisions of Polish Constitution, these entities are guaranteed to participate in public revenues in accordance with their tasks. Income of territorial self-government units is their own income as well as general subsidies and targeted subsidies from the state budget (Article 167, paragraphs 1 and 2 of the Constitution of the Republic of Poland). The sources of income of local government units are defined in the Act of 13 November 2003 on the incomes of local government units (Journal of Laws from 2018 r. pos. 1530).

The real estate tax has a significant fiscal importance in the context of commune income in Poland, especially in the field of buildings related to business activity (Pahl, 2017: 99). A perfect example of this type of construction facilities are wind power plants. The concept of wind power plants is not and has not been defined in the provisions of Polish tax law. The scope of this concept has been defined only in legal acts outside this branch of law. The polish legislator, from 1 January 2017, introduced, by the Act of 20 May 2016 on wind power plants investments (WPI Act – Journal of Laws from 2016 r. pos. 961, as ammended) the definition of "wind power plant" modifying the Act of 7 July 1994 Construction Law (Journal of Laws from 2017 r. pos. 1332 as ammended). At the same time the legislator included a transitional provision concerning taxation of wind power plants. According to art. 2 point 1 of WPI act a wind power plant is a construction within the meaning of Construction Law, consisting at least of a foundation, tower and technical elements, with a capacity greater than the power of microinstallations within the meaning of art. 2 points 19 of the Act

of 20 February 2015 on renewable energy sources (Journal of laws item 478 and 2365 and of 2016 item 925). Nevertheless, it should be underlined that for a building within the meaning of the Construction Law, an "entire" wind farm is considered to be the basis for all its elements and cannot be limited only to the "building" part. This topic provokes passionate discussions in science and practice – it is the subject of relatively numerous, heterogeneous analyzes (Etel, 2017: 13–19, Malinowski, Małecka, 2017: 6–12) and interpretations[10]. It is connected above all with a several-fold increase in property tax on this category of construction works.

Hardly any new taxation rules for wind farms have come into force the new regulations have changed their taxation rules. The amending act was announced in the Journal of Laws in June 2018 and amended the existing regulations with retrospective effect, ie effective from 1 January 2018. Like its "predecessor", it changed the "around tax" regulations without changing the tax act itself. The project justification claims that the entry into force retroactively of changes will automatically change the subject of taxation of property tax based on the Act on local taxes and fees. This fact will have an impact on the amount of taxation on wind power plant property, as this tax will be charged only on their construction parts.

In the authors opinion, it is not true what the legislator asserts in the anticipated effects of introducing new regulations. The legislator points that the entry into force of the proposed regulation will not directly cause the necessity to incur expenditures from the state budget or the budget of local self-government units. The "untruth" of this statement is justified by the fact that from 2017 taxpayers paid the property tax calculated on the value of the whole wind farm. Also in 2018, the tax was paid on the same basis and was transferred as an income of the commune's budget in which the wind farm is located. This means that the entry into force retroactively of the regulations in question results in the need to return significant amounts of property tax. In some municipalities, overpayments on this account may even reach several million zlotys.

10 A different view than the one resulting from the law was expressed in the interpretation of individual tax law regulations issued on 3 November 2016. (mark: FP.310.1.1.2016.2) by the commune administrator of the city of Zgorzelec, repeated in the interpretation of the Commune of the city Puck of 2 December 2016 (F.B 310.2.2016 MW).

The entry into force of the new provisions with retrospective effect, although favourable to taxpayers, constitutes a clear violation of the provisions of art. 2 and art. 167 of the Constitution of the Republic of Poland. This topic should be devoted to a separate study but due to the limited scope of the present article, only basic arguments will be indicated. Namely, article 2 of the Constitution of the Republic of Poland formulates the principle of a democratic state of law (the Republic of Poland is a democratic state of law, implementing the principles of social justice). The rule of non-retroactivity (lex retro non agit) derives from this principle. Normative acts should not apply retroactively. The law must be predictable and inspire confidence in the individuals and parties associated with it. This principle, which has been repeatedly mentioned by the Constitutional Tribunal, is the basis of the legal order resulting from the expression given in art. 2 of the Constitution of the Republic of Poland, the principle of a democratic legal state and influencing other principles, such as the principle of citizen's trust in the state and its law (judgment of the Constitutional Tribunal of 17 December 1997, reference number K 22/96). It should be added that these rules do not apply only to a citizen or a natural person, but they determine the legal situation of other legal entities, including local government units, which in this way are also to be protected from state interference (judgment of the Constitutional Tribunal of 12 April 2000, reference number K 8/98, judgment of the Constitutional Tribunal of 20 January 2010, reference number Kp 6/09). The new regulations introduced in June 2018 affect the property interests of communes whose budgets has already taken into account potential income from wind power plants taxation and, consequently, certain expenses. In this way, the municipalities were deprived of statutorily guaranteed income. It should be noted that draft municipal budgets are prepared and adopted in the year preceding the budget year. The announcement of new regulations in the middle of the financial year destabilized the financial management of several communes. Although the justification for the project has noticed the impact of the new regulations on the amount of taxation of wind farm property, but omitted the element described by the authors, which indicates unreliability of the new regulation.

Art. 17 point 2 of the Act of 7 June 2018 amending the act on renewable energy sources and some other acts that provides the retroactive entry into

force from 1 January 2018 and results in a reduction in the amount of property tax on wind power plants buildings, is also inconsistent with Art. 167 of the Constitution of the Republic of Poland. This provision provides that local self-government units are guaranteed a share in public revenues in accordance with their tasks. Income of local self-government units is their own income as well as general subsidies and targeted subsidies from the state budget. The sources of income of local government units are specified in the Act. Any change in the scope of tasks and competences of territorial self-government units are followed by appropriate changes in the distribution of public revenues. The analyzed constitutional provision formulates the principle of independence of local government units, including the principle of financial independence. The introduction of the new wind power plant regulation retroactively, as a result of which the statutory income from property tax is reduced by law, is a violation of this principle. The above principle, expressed in art. 16 point 2, and then expressis verbis in art. 165 point 2 and art. 167 of the Constitution remains one of the foundations of the existence of territorial self-government. According to the Constitutional Tribunal, the provisions of this article should be understood in two ways. Firstly, as a provision that guarantees communes an appropriate level of income, allowing them to implement constitutionally designated tasks and reserving the form of a law for determining the sources of such income.

Secondly, the significance of art 167 point 3 indicated by the Constitutional Tribunal is to provide the local government unit (…) with adequate financial resources to carry out its tasks. Article 167 point 3 can therefore be treated as an expression of a more general principle, guaranteeing the municipality not only to leave at its disposal certain financial resources (by guaranteeing the sources from which they flow), but also guaranteeing the municipality the ability to use these resources themselves, and thus making expenditures. The fact to exclude the existence of constitutional guarantees for the independence of expenditure, the statutory guarantee of sources of income, as well as the independent performance of tasks could turn out to be illusory, because the obtained funds could be taken to the commune without any restrictions (judgment of the Constitutional Tribunal of 24 March 1998; ref. K 40/97).

7 Conclusions

Legal solutions concerning the taxation of wind power plants in France presented in this paper compared with too frequent changes in the Polish tax system shows a possible violation of the principle legal certainty and the principle of democratic state of law in Poland. It is evident that the lack of stability in the tax regulations is an obstacle for the invertors to engage their founds in renewable energy sources. The French model of taxation is not an ideal one due to the quite big complexity and correlation with several different taxes covering wind power plants. But in the authors opinion the comparative evaluation of one complicated but stable system (French case) and another less complicated but unstable system (Polish case) shows the advantage of the first one. The primary amendments in Polish law resulted at the beginning in the property tax being increased several times and last amendments from June 2018 went in a completely different way by decreasing the value of property tax related to wind power plants. The only advantage of the Polish solutions is related to the fact that polish model is using only one single property tax related to wind power plants. In France, wind power plants are subject to a special tax and have only a subsidiary role property tax, that makes the whole system more complicated and not easy to manage by the international investors.

However if we compare the French system to the Polish one, we see that in France movable and not perpetually fixed parts of a wind power plant were not subject to property tax. However, it was the only possible and economically justified solution because of the fact that in France, a basic wind tax has already been introduced *(taxe éolienne)* and has an annually reviewed rate related to the number of kilowatts of energy that can be generated by a given plant. Meanwhile in Poland, over the last 15 years, the legislator was not sure if both structural and non-structural elements of wind power plants should be subject of taxation or not. In this situation the French model may be an indication for the future for the polish legislator especially in relation to the taxable and non taxable elements of wind power plants related to the property tax and the way that the building being de facto a power plant is understood.

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Insurance Tax in the Slovak Republic[1]

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Abstract

Adoption of the recent legislation on insurance tax has raised many debates in the Slovak Republic. The authors focus on the theoretical definition of insurance, identification of legislation related to the application of insurance tax, and the classification of the subject-matter of taxation. The objective is to analyze the theoretical-legal and application deficiencies of the insurance tax following the abolished levy on part of the insurance premiums in the non-life insurance sectors. It is also necessary to assess the hybrid way of the taxation of insurance, take a position on the possibility of introducing an insurance tax in the Member States of the European Union and point out different regimes for applying this tax in the context of different tax rates and within the scope of the subject matter of taxation. The hypothesis which authors want to prove or disprove is the assertion, if the introduction of this tax has taken into account the theoretical and legal bases for imposing taxes, or it was a political decision potentially conflicting with constitutional law and EU law.

Keywords: Insurance Tax; Insurance; Levy; Non-Life Insurance.

JEL Classification: G10; K34; G18.

1 Introduction

There exists an increasing regulation of social relations arising within the framework of taxation but also in the area of insurance in the current

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legal milieu of the Slovak Republic, of other member states of the European Union, as well as at the level of the European Union itself. The private law nature of the insurance (Štrkolec, 2015: 42) does not prevent the occurrence of many intersections with the legislation of tax law, which is a typical representative of public law. After all, it is precisely the private-law relations that are in principle subject to taxation and form the subject of the relevant tax belonging to the tax system in the Slovak Republic.

Adoption of the recent Law Act No. 213/2018 Coll. on the Insurance Tax and on the Changes of and/or Amendments to Certain Law Acts (hereinafter referred to as the "Insurance Tax Law Act"), valid as of 18 July 2018 and having become effective as of 01 January 2019, extended the tax system of the Slovak Republic by an insurance tax, is an undeniable fact proving this interconnection. However, the process of adopting this tax was preceded by a complicated process by which the Government of the Slovak Republic sought to enforce this tax at any costs, often ignoring the legitimate objections of the entities concerned, who were the most affected by the consequences of introducing this tax.

For a proper understanding of the issue of insurance taxation and the implementation of social relations within its framework, it is necessary to describe the nature of the insurance and its purpose in relation to the insurer and the policyholder or the insured person. Examination of the substance of the insurance relationship shows a number of overlaps in the area of tax law, whereby it is possible to draw conclusions on the necessity or justifiability and correctness of the current legal regulation of the taxation of specific types of insurance in the Slovak Republic.

The primary objective of this paper is to evaluate and analyse the insurance tax in the context of its theoretical-legal aspects and application deficiencies, pointing out the hybrid way of taxation by the tax in question and its possible conflict with European Union law where similar forms of taxation apply.

The authors of this paper use several scientific methods, especially scientific analysis and synthesis, which are complemented by the method of comparison.

2 Definition of insurance basis of its legal regulation and its legislative classification

Insurance (asecuration) may be defined in different ways. Some authors perceive it as an effective form of creation and redistribution of funds that is performed by the insurance agency on the basis of the so-called insurance relationships (Belšínková, 1993: 559), others as one of the forms of financial activity (Karfíková, Přikryl, 2018: 14; Babčák, 2017: 19). Insurance may, however, also be characterized as a contractual relationship between the policyholder and the insurance agency in which the insurance agency undertakes to settle a claim for the insured in the event of an insured event (paper deals exclusively with private-law insurance, not social and health insurance – public insurance. (Boháč, 2013: 193). It is, therefore, a means whose essence is in spreading the insurance claim settlement of one insured on the loss of those insured for whom the insurance claim is not settled because the insured event does not occur.

With regard to the focus of this paper, we consider it necessary to point out the basic legislation governing the implementation of private insurance relations in the context of the adopted Insurance Tax Law Act:

- The primary concern is with the provisions of Sections 788 to 828a of Law Act No. 40/1964 Coll. Civil Code, as amended, where the essential elements relating to actuarial relations, the definition and characteristics of the parties to these relationships envisaged by the Law Act, which are also justified in relation to the Law Act on Insurance Tax, statutory prerequisites for making insurance policies and the rights and obligations arising therefrom, etc. (Števček, 2015: 2859);
- The secondary concern is with Law Act No. 39/2015 Coll. on the Insurance System and on the Changes of and/or Amendments to Certain Law Acts, as amended (hereinafter referred to as the "Insurance Law Act")–this Law Act regulates in particular certain relations related to the establishment, organization, management, and performance of the activities of insurance and reinsurance undertakings, including insurance and reinsurance undertakings from other Member States of the European Union and the countries from

outside the European Union. In connection with the adopted Law Act on Insurance Tax, it is necessary to refer in particular to Section 68a of the Insurance Law Act, which was effective until 31 December 2018, and which was repealed by the Insurance Tax Law Act. The provision concerned the levy of part of the non-life insurance sectors, subject to the transformation process and forming the subject of the current insurance tax (see Chapter 2 for more details);

- Finally, Law Act No. 595/2003 Coll. on Income Tax, as amended (the "Income Tax Law Act") has also to be mentioned – the Income Tax Law Act also amended the Income Tax Law Act, with the possibility, inter alia, of recognizing the paid insurance tax as paid by the policyholder and the tax on insurance from recharged insurance costs under the Insurance Tax Law Act as a tax expense.

From the theoretical knowledge of the insurance system and the insurance, many classifications of this legal institute may be deduced (Ovečková, 1994: 197–203; Belšínková, 1993: 559; Slepecký, 2014: 35–37; Karfíková, Přikryl, 2018: 14–18). However, for the purposes of this paper dealing with the insurance tax, the classification of insurance sectors established by insurance types by the Insurance Law Act will be sufficient in Annex No. 1 (identical in Part A with Annex 1 to the Insurance Tax Law Act):

- Part A - non-life insurance sectors (this part is literally taken over by the Insurance Tax Law Act and forms Annex 1 to this Law Act, the subject of which represents the subject of the insurance tax)– here we include, in particular, accident insurance (including industrial accidents and occupational diseases), sickness insurance, insurance against damage to ground-based motor vehicles other than rail ones, insurance of damage to rail vehicles, insurance of aircraft damage, insurance of floating means of transport, insurance of transport of goods during transport, including luggage and other property irrespective of the means of transport used, insurance against damage to other property caused by fire, explosion, storm, natural elements other than storm, nuclear energy, landslides or soil settling caused by hail or frost, or other causes, such as theft, liability insurance of driving a motor vehicle or carrier, insurance against liability for damage caused by the operation of an aircraft, including liability of the carrier, insurance of liability for damage caused by the

operation of river, canal, lake or sea means of transport, including liability of the carrier, general liability insurance in other cases, credit insurance, guarantee insurance, insurance of various financial losses arising from different life situations, legal protection expenses insurance, and assistance services;

- Part B - life insurance sectors (which forms Annex No. 1 to the Insurance Law Act, but not the Insurance Tax Law Act)–here the law act includes, in particular, survival insurance, in case of death, in case of death or survival, in case of survival with the possibility of reimbursement of insurance premiums, insurance related to capitalization contracts, old-age pension insurance, supplementary insurance made alongside with life insurance, child birth insurance, nutrition insurance and marriage insurance, etc.
- Part C - In this section, the Insurance Law Act generally refers to non-life insurance groups to perform insurance business for the purpose of issuing permits.

3 Insurance tax in the context of the theoretical legal and application deficiencies in respect of the repealed levy of the part of insurance premium from non-life insurance sectors

According to the Explanatory Memorandum to the Law Act on Insurance Tax, the Slovak Government's initiatives to introduce a form of imposition of a monetary obligation on insurers in favour of the State in the provision of insurance services were mainly due to the increasing trend of taxation of insurance services in Central and Eastern Europe. The above need to introduce a specific form of taxation is based, in particular, by the fact that insurance services, pursuant to Article 135(1) (a) of the Council Directive 2006/112/EC of 28 November 2006 on the Common System of the Value Added Tax, are exempt from the value added tax.[4]

From the outset of these considerations, one may observe considerable opposition from the persons concerned. This was mainly concentrated

4 Under that Article, the following legislation has been adopted at European Union level: "*Member States shall exempt the following transactions from taxes: insurance and reinsurance transactions, including related services provided by insurance brokers and insurance agents*".

especially through the interest association of commercial insurance companies – the Slovak Insurance Companies Association (hereinafter referred to as the "Insurance Companies Association"). While receiving the levy of the part of on non-life insurance premiums and transforming it into an insurance tax, they carefully observed the adoption of legislation and subjected it to a critical assessment.

Since 1 January 2017, Law Act No. 339/2016 Coll., Amending Law Act No. 39/2015 Coll. on Insurance and on the Changes of and/or Amendments to Certain Law Acts, as amended, and amending and supplementing certain law acts, became effective that adopted the levy of part of non-life insurance premiums. In particular, that law act as provided for in Section 68a of the Insurance System Law Act regulated that an insurance company, an insurance company from another Member State, and a branch of a foreign insurance company are obliged to pay 8 % of the insurance premiums received from the insurance policies made after 31 December 2016 listed in Annex No. 1 (A) (except for motor vehicle third party liability insurance covered by the 0 % tax rate due to the existence of a special levy for this insurance), while the proceeds of the levy have become a State budget revenue. This regulation has been replaced by the Insurance Tax Law Act and, in view of the direct link between the regulations in question, and their similarity, both the levy and the insurance tax may be subjected to the common assessment. Such a form of burden on insurers was strongly opposed by the Insurance Companies Association, while in its opinion specific reservations were made on this legal regulation[5] which may be supplemented and specified in the context of the adoption of the new Insurance Tax Law Act, largely following the transformation of the tax levy and after the adoption of the law in question.

The first deficiency is in a possible collision with the Constitution of the Slovak Republic. According to that, the State's financial management is governed by the State budget, which is approved by law act, and its income is in accordance with Article 59(1) of the Constitution taxes and fees that

5 For details on the chronology of the comments of the Insurance Companies Association on the payment of part of the non-life insurance premium and insurance tax, see: http://www.slaspo.sk/dan_z_poistenia_vs_odvod

are State and local ones and which may be imposed pursuant to Article 59(2) of the Constitution by law or on the basis of law. Thus, the constitutional authority for imposing the levies is absent in the Constitution itself. In addition, with regard to the wording of the Explanatory Memorandum to the Law Act on Insurance Tax[6] and to the theoretical and legal aspects of taxes (Babčák, 2015: 21–24; Karfíková, 2018: 147–150) and levies, the characteristic of this monetary obligation may in the context of the legislation adopted be considered as a levy rather than a tax (Karfíková, 2015: 36). The above holds true because the levy should have a specified purpose[7] related to the subject of the levy obligation, and even in this case it may be argued whether the imposition of such levies is constitutional.

The second deficiency of the legislation was that the levy was contrary to the rules of fair taxation in that instead of the standard taxation and the application of the Income Tax Law Act, the levy (or tax) in question was applied directly on the company's income without taking into account the eligible costs determined in particular by the Income Tax Law Act. This deficiency has been partly eliminated by the adoption of the Insurance Tax Law Act, which amended the Income Tax Law Act and in the provision

6 In the Explanatory Memorandum on the Insurance Tax, the following is stated: "*The reason for introducing an insurance tax as an indirect tax is topical knowledge showing that the levy on the non-life insurance premiums received as introduced since 1 January 2017 is a non-systemic and ineffective measure causing application problems for insurance companies and unequal treatment in respect of the levy from insurance premiums received under insurance policies made before 1 January 2017 and those made from that date on.*"

7 For the sake of comparison, it is possible to refer to the collected levy from insurance companies and reinsurance companies in the amount of 8 % of the premiums received from compulsory motor-vehicle third party liability insurance from activities performed in the territory of the Slovak Republic, which is levied to a special account of the Ministry of the Interior of the Slovak Republic, while the funds so received will be distributed by the Ministry of the Interior after discussing with the Ministry of Finance to the fire-fighting brigades to cover the costs associated with the acquisition of the material and technical equipment, its maintenance and operation and to the units of the Ministry of the Interior to cover the costs associated with acquiring the technical resources necessary to perform the tasks related to the performance of supervision over the security and smoothness of road traffic, clarifying the causes of road traffic accidents, building and equipping the Integrated Rescue System and emergency calls operating centres and the construction and procurement of technical equipment for the emergency medical service operational centres by the end of June of the relevant year. Such reallocation, also under the Insurance Law Act, is subject to public control pursuant to Law Act No. 211/2000 Coll. on Free Access to Information and on the Changes of and/or Amendments to Certain Law Acts, as amended.

of Section 17(19)(a)(j) of this Law Act it was provided that the insurance tax paid by the policyholder and the insurance tax on the reimbursed insurance costs pursuant to the Insurance Tax Law Act is a tax expense. However, this does not apply to an insurance company which is in practice a standard payer of that tax.

The third deficiency of the levy, but also of the newly adopted tax, is that they appear to be discriminatory due to the determination of the subject of the levy or tax, which are exclusively represented by types of voluntary insurance from the non-life insurance sector without adequate assessment of the economic and social impacts and the negative effects of the levy burden or taxation of this part of insurance. The assessment of this issue is also closely related to the fact that voluntarily insured persons are additionally indirectly sanctioned for their responsible behaviour through possible increases in premiums for insurance policies. Although in principle the insurer is the payer of the insurance tax, it is clear from the nature of the insurance tax that the tax burden is borne primarily by the person who is the policyholder and pays the insurance premium to the insurer.

The fourth deficiency of the tax in question (but also of the levy) may be identified by reducing the transparency of legislation and of the legislator's legislative procedures. In this sense, it may be stated that the fundamental comments of the Association of Insurance Companies were not reflected in any way in the final wording of the adopted legislation on the Insurance Tax Law Act. In any case, ignoring the concise, and often purposeful, observations addressed to the lawmakers to enforce new legislation at any costs without taking adequate account of the concerned persons' feedback does not in any way lead to legislation that contributes to the proper development of not just the entrepreneurial milieu in the Slovak Republic but also of the European Union's internal market.

Other deficiencies of this form of taxation include, for example, the impact on the solvency of insurance companies, the impact on premium pricing, the impact on the business environment (Červená, 2013: 1967), prioritizing policy decisions prior to adopting legislation duly taking into account the current state of the business environment (Románová, 2012: 386), the impact on employment, the impact on life insurance, and so on (Žáková, 2016).

4 Hybrid method of insurance taxation

It follows from the modern theory of tax law that according to the method of taxation, we divide taxes into direct and indirect ones. Direct taxes are those where the taxpayer is identical with the tax liability entity, who, according to the legislator, is supposed to bear the tax on their property and actually pay it, while that person (taxpayer) bears the tax burden. Conversely, indirect taxes are those for which the taxpayer (consumer) and the tax recipient are different entities. The tax burden in this case is borne by the taxpayer (consumer) and the tax to the State budget is usually paid by the person providing the services or supplying the goods. The tax burden is therefore borne by non-taxpayers for indirect taxes (Babčák, 2012: 35–36).

Although the Explanatory Memorandum to the Insurance Tax Law Act states that an insurance tax is a type of indirect tax, it cannot be accepted in full with such a conclusion made by the lawmakers.

In order to demonstrate the above statement, we refer to the wording of provision of Section 4(1) of the Insurance Tax Law Act, under which the insurer is a taxable person, as amended by para. 2(b) of this provision, under which the payer also includes the legal entity to whom the insurance costs are reimbursed as relating to the insurance risk placed in this country and to the wording of para. 3 of that provision, whereby the co-insurer is a taxable person who, under an agreement made by and between the co-insurers, is intended to pay the entire tax if the insurance policy is made by and between the policyholder and several insurance undertakings, insurance undertakings from another Member State or branches of foreign insurance undertakings. It can be agreed that in this case it will indeed be a case of a method of taxation which is characterized by an indirect character, and thus, although the policyholder bears the tax burden, the tax is paid to the State budget by the insurer or co-insurer.

However, this method of indirect taxation is broken in stipulation of Section 4 para. 2(a) of the Insurance Tax Law Act under which the policyholder who has paid the insurance premium to a foreign insurance company that does not have a branch in this country is also a payer; if the policyholder recharges the premium to the legal entity who is the payer, the policyholder

is also a payer to the extent of the premium that it does not reimburse to that person. Based on the basic starting points of the theory of tax law, then, in this case, the method of direct taxation is where the policyholder is the same as the taxpayer. The policyholder therefore bears the tax burden and is also a taxable person.

As per this example, it is necessary to maintain and take into account the knowledge of the modern theory of tax law, which the legislator does not respect many times and neglects to take into account when creating legislation that has a significant impact on the actual wording of the legislation, its justification and its projection in everyday life (for the issue of disregarding the knowledge of tax law theory by lawmakers and legislators in the Slovak Republic, see also Popovič, 2016: 1263–1276).

5 The issue of an option of introducing the insurance tax in the member states of the Euopean Union

As mentioned above, the necessity of introducing special taxation on insurance is mainly based on the fact that under Article 135(1) (a) of the Council Directive 2006/112/EC of 28 November 2006 on the Common System of the Value Added Tax, insurance services are VAT-exempt. However, it is possible to consider why the Member States of the European Union tax the insurance if it is exempt from the value added tax at the European Union level.

It follows from the nature of the insurance that this does not serve as a means of creating added or new values. On the other hand, in the event of an insured event, it is a means of restoring the values that have been destroyed, devalued, or damaged by an insured event. Accordingly, the exemption from the value added tax at European Union level appears to be the right step not denying but strengthening the nature and purpose of the value added tax.

However, after considering the above, a legal question arises as to whether the adoption of special taxes on insurance is not merely a circumvention of the Council Directive 2006/112/EC of 28 November 2006 on the Common System of the Value Added Tax. Despite the fact that this tax is adopted in the form of a special law act that is not at first sight related

to the value added tax, its essentially indirect nature and the payment of the insurance premium tax as a consideration for the provision of insurance services largely reproduces the mechanism of operation of the value added tax. This only supports the fact that the revenue from this tax is not earmarked for the financing of the related State budget expenditure, but is the revenue of the State budget as a whole.

In most Member States of the European Union, income from insurance taxes or from different forms of levy used for specific purposes are closely related to the type of insurance or the subject of insurance. Taxation in these countries is also counterbalanced by various systemic measures (Insurance Companies Association, 2018).

In view of the fact that the insurance tax revenue in the Slovak Republic is not currently tied to a specific type of expenditure related to the subject of taxed insurance and in the context of its similarities with the value added tax, this tax may then be characterized from the theoretical and legal point of view as potentially circumventing the EU law. However, the euro-conformity of this tax is also questionable if the revenue from was also linked to specific expenses related to the subject of the insurance.

6 Comparison of insurance taxes in the member states of the European Union

Taxation of non-life insurance sectors is a widespread practice among the Member States of the European Union. In particular, however, the subject of taxation of non-life insurance sectors and the amount of the tax rate (or another form of imposition of the obligation to pay cash on the liable entities) differ considerably in different countries.

In this sense, the development in question within the European Union may be classified into three groups with respect to the level of tax rates (in the brackets by the name of the State the tax rate is stated) (Bourdaire, 2019):

- Taxation of insurance at high tax rates – in the first group, Member States are characterized by a strong economy and a high standard of living. These include mainly Finland (24 %), Germany (19 %) and the Netherlands (21 %);

- Taxation of insurance at low tax rates – the second group consists of the States at different stages of economic market power and different living standards, such as Denmark (1,1 %), Bulgaria (2 %), Ireland (3 %), Luxembourg (4 %), Spain (6 %), Slovakia (8 %), Belgium (9,25 %), Austria (11 %) and so on.
- Taxation of insurance by different tax rates as regards the subject of insurance – in the last group, the States may be found taxing various types of insurance by different tax rates. This is particularly the case in France, where insurance is subject to taxation at a tax rate of between 7 % and 30 % and Italy, where insurance is taxed at rates of between 0,05 % and 21,25 %.

However, it is necessary to point out that, as the tax rate varies from one Member State to another, the subject of taxation also varies or what also varies is the fact of which sector is subject to the relevant tax rate in the relevant Member State. In this context, the following breakdown may be pointed out (www.abi.org.uk) in the context of the data available:

- No subject-matter to taxation of the non-life insurance sectors – in Estonia, Lithuania, Latvia and the Czech Republic, insurance is not subject to taxation;
- The narrow subject-matter of insurance sectors of non-life insurance – for example, in Finland, there is a fire insurance and insurance against damage caused by the use of the means of transport, in Sweden insurance against damage caused by the use of the means of transport is taxed, in Poland there is a fire insurance;
- The broad subject-matter of taxation of insurance sectors of non-life insurance – in other Member States of the European Union, the subject-matter of taxation is more or less extended to all of the non-life insurance sectors.

7 Conclusion

The new Insurance Tax Law Act, which was preceded by legislation providing for the levying of part of the non-life insurance premium, has raised many questions and a wave of displeasure, not only from the public but also from the stakeholders involved in the Insurance Companies Association.

This paper identified a number of particular deficiencies in the tax legislation concerned (including its historical predecessor) in question, which was largely pointed out by the persons concerned before the adoption of the applicable and effective legislation, but which is not and has not been taken into account by the legislator and the government. The same applies with regard to the similar tax treatment scheme in other Member States of the European Union, which even the lawmakers referred to in their Explanatory Memorandum.

Conformity of the Slovak Insurance Tax Law Act with the European Union law also seems questionable, namely Council Directive 2006/112/EC of 28 November 2006 on the Common System of the Value Added Tax, which exempts insurance services from the value-added tax scheme, taking into account the actual nature and the effective application of the Insurance Tax Law Act in practice.

The result of the research into and reflection on the aspects of the new insurance premium tax in the Slovak Republic taxation system is a fact that has been pointed out by many authors of modern tax law for many years. Many times, the legislator does not respect the theory of tax law known for a long time and uses terminology in this sense and purposefully creates legislation that does not correspond to that knowledge. This results in opaque, unsystematic, ambiguous, and complicated legislation.

Such a lax approach, without taking into account the available scientific knowledge and without taking into account the concerns of the persons concerned, may also lead to the adoption of legislation that adversely affects the business of the actors concerned, restricting tax competition within the European Union's single internal market, social and economic interventions of individuals and so on.

One may think about whether the adoption of the Insurance Tax Law Act without a broad society-wide debate, the conclusions of which would actually be reflected in the wording of the Law Act, was the best solution and it is not justified currently. This reflection may also be applied to the fact whether it is necessary to penalize the responsible behaviour of policyholders who prevent the occurrence of damages by insurance of property, which might not be remedied and removed under any other circumstances.

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INTERNATIONAL TAX LAW

On the Issue of Tax Crimes

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Abstract

The subject of this study is the study of the theoretical foundations of tax crimes in the Russian Federation. The relevance of the chosen topic is not in doubt, since the current tax practice has to deal with tax crimes of various kinds. The study of the causes that contribute to the development of tax crimes should be given great importance. To date, the tax legislation is constantly being amended, which necessitates new scientific developments in the field of tax crimes. Today, effective measures to combat tax crimes aimed at minimizing the financial losses of the budget system are appropriate. It should be recognized that work in this area is not sufficiently active at the moment. Different economic methods were used in this study. Thus, on the basis of the method of observation and collection of facts, the reasons for committing tax crimes in Russian practice are studied in detail. Using the method of synthesis and analysis, system-functional method, the article presents analytical data on the issues under consideration. The authors identify relevant conclusions that are aimed at the application of effective measures to reduce tax crimes by using the method of scientific abstraction. The study suggests that the priorities of the tax authorities have now changed, namely, inspections of enterprises, organizations and individual entrepreneurs are carried out not by random sampling.

Keywords: Tax Crime; Tax Investigations; Tax Legislation; Tax Potential.

JEL Classification: H21; H22; H26.

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1 Introduction

In the current tax practice have to deal with tax crimes of various kinds. Currently, the criminal legislation of the Russian Federation includes four elements of tax crimes: tax evasion and charges from individuals (citizens), tax evasion and charges from organizations and enterprises, failure to fulfill the duties of a tax agent, concealment of funds or property of an organization, enterprise or individual entrepreneur, at the expense of which taxes and fees should be collected.

It is well known that a tax crime is understood as a guilty socially dangerous act in the field of taxation, for the Commission of which the criminal legislation of the Russian Federation provides punishment.

It is important to note that the increasing dynamics of tax crimes is accompanied by unfavorable processes in the economy. It is tax crime that is the result of complex economic and social processes that arise from the interaction of certain persons in the course of activity.

The study of the causes that contribute to the development of tax crimes should be given great importance. It is important to recognize that work in this area is not sufficiently active at the moment. The reasons for committing tax crimes are divided into the following groups: economic, political, technical, legal, social reasons. We give a brief description of each group.

Economic reasons for tax crimes arise in the case of a reduction in the level of production, reducing the profitability of organizations and enterprises, the export of capital from the country, financial despair, leading to crimes. (Artemenko, Artemenko, 2018: 327–330) Financial insolvency of a person (both physical and legal) provokes illegal actions, non-payment of tax payments, and, as a consequence, tax crimes. A serious economic reason for tax crimes is mainly the fiscal direction of tax policy, which encourages taxpayers to hide income and bypass the payment of tax payments.

The political causes of tax crimes are manifested at a time when the state is pursuing an economically unjustified policy. (Aguzarova, Aguzarova, 2018: 201) Tax policy should be consistent with the General policy of the state. It should be noted that with the aggravation and destabilization

of state power, there is a decline in the level of collection of tax payments due to the failure of taxpayers to fulfill their tax obligations to the state.

Tax crimes can be committed for technical reasons. These include imperfection of forms and methods of tax administration and control. In this case, we are referring to the insufficiently developed mechanism of external control by tax services with other interacting state services. Technical reasons also include non-compliance or complete lack of material and technical equipment (for example, the presence of outdated office equipment, lack of personal computers), lack of digital software and information technologies (for example, software for accounting, storage, transfer of accounting and tax reporting data). In the modern world, it is information and technical support that is recognized as the basis for establishing the fact of a tax crime. (Artemenko, Artemenko, 2018: 167–170) With the help of innovative software products it is possible to identify tax crimes and effective measures to prevent them.

At the same time, among the reasons for committing tax crimes, first of all, it is necessary to highlight the legal reason, since the tax is not only an economic, but also a legal category. The legal reasons for tax crimes include imperfection and instability of tax legislation. As you know, tax legislation is the most mobile. It is changing more than any other area, which creates serious difficulties in practice. In addition, in the course of tax services use a considerable number of legal acts having the force of law, such as orders, instructions, explanations. They are created not only by the Federal tax service of Russia, but also by the Ministry of Finance of Russia, as well as by the bodies of the judicial system of Russia, etc. Certain norms of tax legislation are contradictory and not coordinated. Insufficiently precise provisions of the legislation give grounds for their double interpretation. For example, there are many contradictions in the mechanism of calculation and payment of value added tax, which makes it possible to make illegal tax compensation provided by tax legislation.

Social causes of tax crimes can be manifested in the behavior of a person in terms of his solvency. For example, when a person is not satisfied with his social status. For example, family problems associated with the financial situation, leave no opportunities for payment of tax payments to the budget system.

Thus, on the basis of our study, we have identified the reasons that provoke tax crimes: the unfinished rules of tax legislation, the complexity and ambiguity of the interpretation of certain provisions of the legal framework; gaps in the work of tax services; the impact of the General policy of the state in General on tax policy in particular; concealment of available income for the purpose of non-payment of tax payments; the reluctance of taxpayers to fulfill their direct tax obligations confirms the low level of tax culture and discipline; ignorance of taxpayers of the rights, duties, responsibility, obligations to the state; imperfect interaction of tax services with other state bodies; weak material and technical equipment in tax services; low financial condition of enterprises and organizations.

As a result of the study of the causes of tax crimes, we found that their number tends to decrease. This is a great merit of the tax authorities.

2 Results

The Federal tax service systematically reduces pressure on business, concentrating efforts on areas of maximum risk, minimizing administrative pressure on bona fide taxpayers. Due to the use of "big data" technology, the approach to conducting inspections has been conceptually changed and the influence of the human factor has been minimized. And the use of risk-based approach in the selection of objects for on-site tax audits (GNP) since 2007 allows for a number of years to improve their efficiency while reducing the number of inspections.

In General, from 2010 to 2018 the number of on-site inspections decreased by more than 5 times. In 2017, 20,2 thousand on-site tax audits were conducted, which is 5,9 thousand, or 22,6 %, less than in 2016 (26,1 thousand inspections). In 2018 14,2 thousand field tax audits were conducted, which is 30 % or 6 thousand checks less than in 2017.

According to the results of on-site tax audits for 2018, 307,6 billion rubles were added, which is 0,8 % lower than in 2017 (310 billion rubles). At the same time, the efficiency of one effective GNP increased by 14,8 % compared to 2016 and amounted to 15,7 million rubles by the end of 2017 (in 2016 – 13,6 million rubles per one inspection). And at the end of 2018,

the efficiency of one effective GNP amounted to 22,2 million rubles, which is 41,8 % higher than in 2017.

Most notably you feel the reduction of the administrative burden taxpayers, applying special tax modes, and traditionally referred to the category of small business – audit coverage this category of taxpayers was reduced even more.

So, if in 2010 three taxpayers out of 1000 were checked, in 2017 the tax service checked one out of 2000, and at the end of 2018 – only one representative of small business out of 4000. Thus, the coverage of small business inspections for 8 years has been reduced by 12 times (from 0,3 % in 2010 to 0,025 % in 2018).[3]

The main focus of the Federal tax service is not on improving the efficiency of one GNP, but on the growth of current tax liabilities of taxpayers, including those who refused to use schemes to minimize tax liabilities, by improving tax administration and reducing the tax gap.

As a result of the work carried out in 2017, without the appointment of inspections, more than 56 billion rubles were additionally received by the budget, which is 2 times more than in 2016 (27 billion rubles). At the end of 2018, the share of these revenues amounted to 27 % of the total budget revenues as a result of control and analytical work (80 billion rubles).

Tax investigation is essential in the detection of tax crimes, the conduct of which is possible only in respect of violations of tax legislation. (Pochueva, 2019: 116–117)

Tax investigation is a set of various measures, both investigative and analytical, with the help of which the appropriate public authorities study all the circumstances and conditions of committing tax violations that counteract tax legislation. Tax investigation is a complex of law enforcement and other functions, where the fundamental factor is recognized as an illegal act, qualified as a tax crime.

It is important to note that the tax investigation is a kind of law enforcement investigation of the state, which combines elements of administrative, criminal, procedural types of investigation. In the event that the action took

3 Available at: http://www.nalog.ru

place in the tax area, the clarification of the circumstances and conditions in such a case becomes possible through a tax investigation.

The tax investigation is closely connected with the activities of the tax services in terms of control work, as well as with the Ministry of internal Affairs. Tax investigation is an independent institution that links the process of tax control and tax crimes. (Sukhodolov, Popkova, Kuzlaeva, 2018: 55–59)

Specific features has an investigation of tax crimes on evasion of tax payments regarding the establishment, introduction and collection of taxes and fees, as well as the implementation of tax administration and control over enterprises and citizens.

The investigation of tax crimes is carried out in several stages. The initial stage of investigation of tax crimes is seizure of documents and their inspection; search. Documents relating to the accounting of transactions in credit and financial institutions used by the enterprise should be withdrawn. Seizure of office equipment can be made in the tax investigation. The search is carried out to identify the material that helps to solve the tax crime.

An important stage in the investigation of tax crimes is the interrogation of persons involved in the case. So, the interrogation of experts, witnesses, suspects, accused is the most common and effective investigative action in the investigation of crimes on taxes and fees.[4]

With regard to the investigation of tax crimes revealed in the course of the GNP, we note that the investigating authorities in 2018 sent 3,8 thousand materials (including under article 32 of the tax code of the Russian Federation – 3 thousand materials under article 82 of the tax code – more than 800 materials), by results of consideration of which more than 1,4 thousand criminal cases in connection with the presence of sings of tax crimes under the criminal law were brought (article 198–199.2 of the criminal code).

The share of refusals to initiate criminal cases decreased by 6 percentage points to the level of 2017 and amounted to 51 % (in 2017 – 57 %). At the same time, the share of refusals to initiate criminal cases is reduced annually.

4 Available at: https://medium.com/@taxcrimeinvestigation1/tax-crime-investigation-how-to-lower-the-risk-and-probability-808b88c4dd32

Thus, if in 2011 a criminal case was initiated only for every tenth material sent by the tax authority, in 2018 – almost every second material.[5]

The amount of compensation for damage caused to the state as a result of the investigation of criminal cases in 2018, according to the materials of the tax authorities, amounted to 18 billion rubles (in 2017–19 billion rubles).

It should be noted that the tax investigation has the following features: it is based on the methods and ways of operational, investigative, criminal, procedural nature, as well as the results of tax administration and control; it is aimed at ensuring law and order in the tax field and protecting economic and tax security.

Thus, these data indicate that today the vector of work has changed: inspections of enterprises are carried out not by random sampling, but in relation to those who have a high risk of using illegal tax optimization schemes.

However, today there are new types of crimes that occur with the introduction of electronic money, Internet transactions, etc. Crime became organized, professional, international. (Sakharov, 2019: 184–188)

The peculiarity of the mechanism of tax crimes is, among other things, the fact that the methods of their Commission and concealment mostly converge. The essence of their Commission and concealment is, first of all, the submission of invalid information to the tax authorities.

Investigation of the causes of tax crimes will make it easier to solve the problem of their elimination, as well as identify ways and methods of combating illegal actions.

As practice shows, the Commission of tax crimes often occurs from the moment of entering into the financial and accounting statements of incorrect data on income or expenses, as well as from the moment of concealment of objects of taxation and ends with evasion of tax payments.

It is important to note that in the investigation of tax crimes interrogated persons may distort the facts. (Novikova, Sukhov, 2019: 119) Therefore, the primary task of the investigator in this case is to reveal the true materials of the case by any means.

5 Available at: http://www.nalog.ru

3 Conclusions

Summing up the results of the study, it should be noted that tax crimes are a type of crimes in the field of economic activity that infringe on the financial system of the state. The reasons for committing tax crimes are divided into such groups as: economic, political, technical, legal, social. The basis for a crime in the field of taxation can be complex and contradictory rules of tax legislation; imperfection in the activities of tax authorities; tax evasion; low level of tax culture; inadequate to modern standards of material and technical equipment and others.

The study of analytical material on the topic of the study revealed that the Federal tax service reduces the pressure on business, reducing administrative pressure on bona fide taxpayers. The approach to carrying out checks is changed and influence of a human factor is minimized. The number of on-site inspections has decreased, the effectiveness of one effective GNP has increased. The main focus of the Federal tax service is on the growth of current tax liabilities of taxpayers.

The study of the current state of tax crimes confirm that the effectiveness of criminal and procedural activities of law enforcement agencies in this category of cases depends largely on the reliable submission of information to the bodies of inquiry to investigate the decision on the initiation of criminal proceedings.

Today, certain provisions of the criminal law (articles 198 and 199) remain unclear, which makes it expedient to develop sound methodological recommendations containing criteria for the legal assessment of the investigation of information about crimes committed in the field of taxation.

It is important to note that any fact of a crime must be supported by evidence of its Commission. The body of inquiry is obliged, within the framework of operational investigative activities, to carry out appropriate measures for its identification, suppression and disclosure of cases. To do this, first of all, it is required to establish the existence of a crime (for example, non-payment of tax within the statutory period).

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Treaty Shopping as a Special Form of International Tax Optimalization

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Abstract

The subject matter of the article is international tax law in the context of tax optimization. The treaty shopping construct undergoes analysis. Treaty shopping is used by international holding companies as part of their tax strategies. It is often adopted in tax haves with double taxation avoidance agreements used simultaneously. The tax aspects of treaty shopping are significant not only from the point of view of analysis of internal domestic tax law applicable in individual countries but also from the perspective of international tax law. The article focuses in particular on comprehensive presentation of the legal and illegal techniques employed within the framework of treaty shopping.

Keywords: Tax; Treaty Shopping; International Tax Law; Corporate Income Tax.

JEL Classification: K33.

1 Introduction

Appropriate use of the applicable agreements on the avoidance of double taxation is essential for holding companies to internationally optimize their tax policies. However, occasionally the law is used for the purpose of international tax optimization in a manner inconsistent with its original purpose. This is primarily connected to so-called treaty abuse and the use of an AADT's (Agreements on Avoidance of Double Taxation) provisions by entities not entitled to do so (also known as treaty shopping).

In general, the phenomenon of treaty abuse is concerned with inappropriate use of an agreement's provisions, where "inappropriate" does not necessarily denote the commission of an offense or a formal breach

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of an AADT's provisions. Therefore, treaty abuse is often referred to as the improper use of a treaty on the avoidance of double taxation. Treaty abuse may thus refer to various situations that require a definition, each of which lead to specific legal consequences.

One of the main objectives of the present elaboration is to demonstrate the role of treaty shopping in the tax strategies devised by international holding companies. Undoubtedly, to this end, it will be helpful to systematize the role of treaty shopping and the differences between treaty shopping and treaty abuse. Another important objective of this paper is to indicate the factors exerting key influence on the effective use of treaty shopping. And in this context, it will be useful to analyse both the legal and illegal techniques employed for these purposes.

In consequence, the above-mentioned objectives of this elaboration will allow to support a thesis the the instrument of treaty shopping is more and more effectively adopted for the purpose of tax optimisation by holding companies conducting cross-border operations. The varied tax regulations applicable in different countries as well as the constantly changing forms of avoidance of double taxation agreements contribute to the effective use of treaty shopping.

2 Treaty abuse and tax avoidance

Treaty abuse may be discussed from two perspectives:

- abuse of an agreement's provisions by one state-party to the agreement; or
- abuse of an agreement's provisions by legal persons who may or may not intend to obtain a greater benefit than available pursuant to the context and nature of the AADT.

Abuse of an AADT by a state-party to an agreement occurs when a state uses the right to freely shape its domestic tax law to modify its obligations to a state (i.e., the other party to the agreement), which results in an upset of the balance between the tax-related powers under the AADT. One must note, however, that this type of abuse does not directly influence an international holding company's situation. Although such companies may still

indirectly reap the benefits of the situation, such benefits are not caused by their actions (Baumgartner, 2016: 234–235; Zdyb, 2007: 13–17).

Conversely, abuse of the provisions of an AADT by entities other than the state-parties may take two forms:

- a situation in which the primary intention of using an AADT is tax avoidance in one country (e.g., the source state) or in both countries (the source state and the state of residence), which leads to an erosion of the expectations and tax policies of the states-parties to the AADT and consequently, to distortion of the purpose of avoiding double taxation in a broad sense; and
- treaty shopping (Lang, Pistone, 2010: 67–71).

The phenomenon of treaty shopping is concerned with particular financial actions (i.e., financial operations) outside the borders of a taxpayer's state that consist of applying the provisions of a control AADT and consequently, gaining advantage in the form of a reduction in foreign tax.

International tax-law doctrine provides several slightly differing definitions of this phenomenon; however, the nature of treaty shopping involves an entity not entitled to the benefits of an agreement using another entity to achieve its aim. To recap, one might state that treaty shopping is the practice of using an AADT by making transactions or establishing entities in other states exclusively for the purpose of using the AADT's provisions that apply to relationships between an involved country and the third country. The agreement in question could not be applied in any other case because the entity making use of the preferential conditions is not a resident of a state that is a party.

The phenomenon of treaty shopping combines the elements of tax avoidance and the use of not only tax treaties but also tax havens' statutory regulations.

The proper use of the applicable AADTs remains an essential issue in the field of international tax planning. The reason for treaty shopping is the incompatibility between the systems for bilateral agreements on tax avoidance and the development and needs of global trade. This conclusion also applies to the differences between national tax laws and the provisions of tax treaties because each tax convention is negotiated by its

parties, which means that residents of particular countries may use diverse tax privileges. If there is no AADT between the state of an investor's residence and the source state, the investor may make an investment through a third country, if that country has entered into a bilateral agreement with the source state to avoid double taxation. A similar case occurs when a tax treaty between an investor's state of residence and the source state stipulates lower tax benefits than does another AADT concluded with a third country. This is especially relevant with respect to withholding-tax rates. All of these circumstances foster tax planning that in reality is nothing but classic tax avoidance (Wyściślok, 2006: 15).

It is noteworthy that treaty shopping is concerned exclusively with the use of tax treaties by persons who are not within the personal scope of such agreements. Accordingly, the phenomenon occurs when a nonresident of a state-party to an AADT establishes a company (or a different undertaking) in that state solely to benefit from a bilateral agreement to which the state is a party. Accordingly, treaty shopping results in the inclusion of a nonresident into the personal scope of an agreement only for the purpose of gaining the otherwise unachievable tax benefits arising from that agreement. This type of practice is enabled by the failure of the taxpayer's state of residence to conclude an agreement with the source state or its conclusion of a less-advantageous agreement than the one the taxpayer intends to use to obtain more positive tax consequences. If no limitations existed with respect to this strategy, a foreign entity might reduce the tax base of a domestic entity by paying interest or royalty payments, mutual setoffs, or other deductions, all of which are advantageous in terms of tax (Lang, Pistone, 2010: 67–71).

Bearing in mind the definition of the phenomenon of treaty shopping provided above, one might wish to examine the difference between treaty shopping and treaty abuse. Treaty shopping is nothing more than seeking a more advantageous AADT and should not be equated with treaty abuse. Accordingly, classifying a given situation or use of an AADT by an entity as abuse requires that each situation be verified to determine whether an indirect (or rarely, direct) breach of an AADT's provisions has occurred with respect to its personal scope, nature, or objective, which is difficult to do *a priori*.

The OECD has also identified treaty shopping as the inappropriate use of an AADT (either by a resident or a nonresident) for the purpose of using the tax preferences arising from it through an entity legally established in a state-party where such privileges otherwise could not be used directly.

It should be stated that treaty shopping is undesirable for the following reasons:

- tax preferences arising out of agreements negotiated by states are economically stretched to the residents of a third state, which is inconsistent with the intention of the states-parties to an AADT and causes, inter alia, a disturbance of the tax balance achieved by means of this AADT;
- income "circulating" around the world either may be taxed inadequately considering the intentions of states-parties to an AADT or may even not be taxed at all, which is unacceptable because the central principle of an AADT is the exemption of income from taxation in one country if it has been taxed in another; and
- a state whose residents treaty shop has no need to enter into an AADT with other states because its residents "use" the protection granted by agreements to which the state of residence is not a party (Bhala, 2015: 112).
- Treaty shopping is a very profitable form of accomplishing the objective of avoiding taxation by using foreign tax laws that grant privileges. This action is much more advantageous, safe, and effective than attempts to achieve this objective on the territory of a single state. Treaty shopping may be accomplished using various financial techniques and tax authorities find some of those techniques more acceptable than others (i.e., legal versus illegal techniques). The difference between these two types of treaty-shopping techniques lies in the form of a legal act employed for the purpose of reducing a tax burden: one must remember that if the form of a legal act dominates its substance, a tax-law violation has occurred. This leads to the conclusion that treaty-shopping financial techniques whose form dominates over substance are considered illegal because they create legal relationships devoid of any economic basis. Their only goal is to reduce tax, which is tantamount to abuse of the tax law (Arnold, 2019: 345–347).

3 Legal techniques

Legal techniques for treaty shopping assume three distinct forms. These forms have been identified based on a criterion of gaining tax residency in a state that is a party to an AADT and include the following:

- the direct conduit method;
- the back-to-back loan method; and
- the stepping-stone method.

The application of these techniques depends on a transaction's purpose, the types of companies in a holding structure, and the type of income that is to be receive preferential tax treatment through an AADT (de Broe, 2008: 58–60).

The direct conduit method – also referred to as the direct method – is adopted when an AADT applicable on the territories of two states allows an exemption from withholding tax in one country for dividends paid by a company with a registered office in that country to shareholders in the other country.

This method is used when a company that is a resident of one country makes an investment in another country and either there is no AADT applicable to the relationships between these two states or such an agreement has been concluded but does not offer any substantial benefits. Thus, to obtain tax benefits, a conduit company is established in a country that has entered into an AADT with advantageous tax provisions.

Another legal treaty-shopping technique is the back-to-back loan method, which is employed to transfer the interest on loans granted by associated economic entities. Fundamentally, this method is only adopted when one company will loan money to a company with which it is financially or economically associated. Consequently, income may be transferred to another country and an AADT's legal regulations exempt that income from tax. It is noteworthy, though, that some representatives of the doctrine consider this method as merely a specific type of direct conduit.

The third legal treaty-shopping technique is the stepping-stone method, also referred to as the indirect method. This method might also be defined as an extension of the method of direct conduit. It consists of establishing a second conduit company in a fourth state that has entered into a more

advantageous AADT with a country in which a particular investment is to be made. Thus, two conduit companies are established: one in the third country and the other in the fourth country. The role of these companies is to transfer income from a holding company's country of residence to the country where the investing company is situated. This method is most frequently adopted when income is generated by a company with a registered office in a high-tax country (de Roni, 2015: 112).

The basic difference between the direct conduit and stepping-stone methods is that the direct conduit method is based on tax exemptions – i.e., using tax exemptions in the conduit country – and the stepping-stone method consists of reducing the amount of tax in the conduit country through the mutual offsetting of expenses. Companies used for the purpose of adopting the stepping-stone method generate profit for the following reasons: they may exempt all of the incurred expenses; the country where the company has its registered office does not impose a substantial withholding tax on income transferred abroad; or income received by these companies is exempt from withholding tax in a foreign country under the provisions of a bilateral agreement.

Two types of companies are employed in treaty shopping, namely, base companies and conduit companies. To use the tax privileges available in a given state, such companies have registered offices in countries that have entered into many tax treaties, many of them tax havens, whether no-tax, low-tax, or special tax havens. A base company is intended to conduct certain activity in the interest of an associated entity in a high-tax country. Its legal form is used to minimize tax in the country of an investor's residence, whereas its main function is to redistribute income received from the associated company to its shareholders – residents of another state. Conversely, the conduit companies are used to obtain tax benefits in a source country where the actual economic substance of an investment is localized. In some cases, the same structure may be employed for both of the presented purposes. Therefore, some of the companies used for treaty shopping may be treated both as base and conduit companies depending on the transaction in which they are currently involved (Panayi, 2008: 234).

All of the methods of treaty shopping have one feature in common. This feature is manifested through the so-called financial conduit or a conduit entity with residency in a country that has entered into an advantageous AADT. In the case in question, the extent of a conduit is influenced not only by its nature but also by its degree. Because of their tax-related objectives, some companies do not conduct actual business activity; therefore, they are not equipped with the necessary resources to do so (which is typical for holding companies). Others, however, play the role of an international company's regional center. However, there is no consensus as to what type of business activity a conduit company should undertake for the tax authorities to classify it as a base or a conduit company (Zdyb, 2007: 16).

Moreover, a taxpayer may use a direct conduit to shift income from the source state to a recipient, the so-called beneficial owner. However, it is necessary to establish a company or other entity in order for the conduit to act in a state that has concluded an AADT that is advantageous to the taxpayer. It is also important for a taxpayer to use the preferential exemption of taxation resulting from statutory tax regulations in a state where a company has been established. In summary, one should remember that two conditions must be jointly observed for an intended undertaking to turn out successful:

- a conduit entity should use its tax exemption in the country where it has been established; and
- income should be transferred through a conduit entity to the so-called beneficial owner with minimal withholding tax collected at the source (Panayi, 2008: 238).

Moreover, a conduit company may also be extremely useful in altering the character of received income on its "way" from the source state to the beneficial owner. Under different circumstances, a conduit company may be employed to obtain the tax benefits arising from an AADT even in a situation in which a company's income is subject to full tax liability in a high-tax state if it is permitted to deduct certain costs by state's statutes.

4 Illegal techniques

Furthermore, several illegal techniques may be adopted when treaty shopping. Illegal techniques involve using an AADT unlawfully. One must remember, however, that because of the character of some of the EU Member States' national statutes, such techniques are not deemed illegal. These techniques include the following:

- the technique of double tax residency and transfer of tax residency;
- 'triangular cases';
- rule shopping;
- shifting to a lower tax bracket; and
- dilution or splitting (Zdyb, 2009: 29–30).

The techniques of double tax residency and transfer of tax residency consist of alternating a taxpayer's tax residency. According to the OECD Convention, transfer of tax residency occurs when, to sell shares and avoid tax on income generated from asset sales, a taxpayer with tax residency in a state party to an agreement on avoiding double taxation transfers its tax residency to a different country where profit is subject to low or no tax. The technique of double tax residency consists of minimizing a company's tax burden by manipulating the tax residency of companies, where each has a registered office in a different state-party to an AADT. This technique may involve changing an original dividend between companies located in two countries into a dividend payment between companies with tax residency in only one state. The change in tax residency described above is apparent and made only to achieve tax optimization, which is tantamount to a breach of tax law.

Next, 'triangular cases' involve using an establishment (or a subsidiary) and the rules for the taxation of an establishment (or a subsidiary) based on an AADT under the following circumstances: an establishment (or a subsidiary) is situated in a country that imposes no tax on its income, if generated in a foreign source state; the source state is a tax haven and the state of residence of the company that owns the establishment does not tax the company's profit earned by its foreign establishment. This practice may be considered to be on the verge of infringing tax law because it may

lead to paying no tax at all on the generated income. This is especially undesirable from the perspective of countries that would otherwise receive financial resources from taxing an establishment's income (Maisto, 2006: 224).

The technique of rule shopping consists of changing the character of income. Its primary purpose is to convert one type of income to another that is subject to more advantageous tax rules under agreements on the avoidance of double taxation. The technique of rule shopping is usually concerned with:

- conversion of gains from real property to gains from shares;
- conversion of dividends to capital gains;
- conversion of dividends to interest; and
- so-called derivative transactions.

Conversion of gains from real property to gains from shares consists of alienating real property situated in a state different than the investor's state of tax residence. In line with the OECD MC, the right to impose tax on the gain from alienating real property is assigned to the country where the property is situated. If such alienation takes place and an AADT between the source state and the state of residence has been concluded based on an OECD MC, then gains from alienating shares in real property are subject to taxation in the alienator's state of residence. Therefore, taxation may be avoided in a country where real property is situated by establishing a company that will own (directly or indirectly) shares in the real property (Maisto, 2006: 263). In the newest version of the OECD MC, this provision has already been formulated differently and stipulates that gains achieved by entities with a registered office in one state due to the transfer of shares constituting over 50 % of the value of real property situated either directly or indirectly in the second state may be taxed in the second state. Introduction of the new version of the provision was intended to hinder conversions of gains from real property to gains from shares. However, there is a way to circumvent this regulation by engaging in so-called dilution or splitting. Thus, it might be stated that the emerging solutions adopted to avoid taxation reflect the needs arising from those provisions (Arnold, 2019: 352; Zdyb, 2007: 27).

Conversion of dividends to capital gains may be performed in a situation in which an investor in one country is in possession of controlling shares in a company that is a resident of another state, and an AADT concluded between these states provides for withholding tax on dividends but not on the transfer of capital gains. Therefore, if an investor needs cash inflow, it may – instead of waiting for dividends to be paid out to shareholders – sell off some of its shares. Simultaneously, an investor maintaining control over a company may produce the effect of converting dividends to capital gains by selling only some portion of the shares. Such a solution is also advantageous because the investor may repurchase the sold-off shares from the buyer by initially entering into a repurchase agreement. The repurchase transaction may also be beneficial for the buyer because it can incur a capital loss that it may later utilize in a different way. This situation takes place when an investor sells its shares immediately before the ex-dividend date and repurchases them early enough for the market price of the shares to fall by the amount of the dividend to be paid out. In such a case, the share seller incurs capital losses in the amount of the dividend.

Conversion of dividends to interest may occur when an AADT does not provide for the taxation of dividends with withholding tax or when such taxation is more advantageous than it is in the case of divided distribution (Arnold, 2003: 32; Martinem Ramirez, 2002: 623; Pistone, 2006: 4).

Using derivative transactions allows holding companies to use the treaty benefits offered by an AADT, primarily with respect to the taxation of capital gains and interest. Such a situation arises because derivative transactions based on the formal character of income enable the achievement of the same results as transactions whose economic substance prevails over their legal form.

Another rule-shopping technique is the so-called shifting to lower tax bracket, which consists of manipulating transactions to subject income to taxation at the lower rate of two different tax rates stipulated by an AADT for this type of income. Such a situation occurs with respect to dividends: when a shareholder wants to benefit from a lower withholding tax rate, it raises the value of its shares in a company's capital before distributing the dividends. Simultaneously, one must remember that a shareholder need not

directly raise the value of shares because it may establish a holding company for this purpose and contribute its shares to that company. Such a practice violates the provisions of an AADT (von Thulen Rhoades, Langer, 2017: 243).

The final technique is so-called dilution or splitting. The objective of this method is to reduce the tax base in the source state. This action may be useful in the case of capital gains taxation because the right to tax gains from transferring shares whose value amounts to 50 % of the value of real property situated one state is assigned to that state. Real property may be divided into several parts so that the value of each part is adequately diluted for tax purposes, causing income derived from alienation of that real property to be not subject to taxation in the source state. In such a case, the source state will be deprived of the possibility of taxing income from the alienation of real property due to tax base reduction caused by dilution of the value of real property performed solely for tax-optimization purposes. Therefore, dilution or splitting may be regarded as a method that breaches an agreement on the avoidance of double taxation (von Thulen Rhoades, Langer, 2017: 245).

5 Conclusions

Successful treaty shopping results in the following benefits:

- reduced tax in the country-source of income;
- a low or zero tax rate in the country of the income beneficiary; and
- low or zero tax rate in the country of the entity that actually receives income.

The first advantage arises from tax treaties that avoid double taxation by stipulating a low or no tax on certain incomes (e.g., dividends) in the country where they are generated. The second advantage is obtained in a tax haven that offers advantageous tax rules for certain forms of activity, especially activity conducted by holding companies. The final advantage arises out of a tax haven's failure to impose a withholding tax in the place where the profit is earned (with respect to distributed profit).

To attempt to explicitly appraise whether treaty shopping is a negative phenomenon, one must examine the bigger picture. Treaty shopping is an instrument that taxpayers may use to reduce their tax burden through the correct use of an AADT. From many interest groups' perspective, such a phenomenon is nothing more than tax avoidance on an international level. The basis of treaty shopping is the use of certain AADTs by entities that are not permitted to do so. The nature of treaty shopping consists of combining many mechanisms and instruments of international tax law. The correct use of such agreements as part of a tax optimization policy pursued by holding companies offers them an important instrument for reducing or even completely avoiding tax. Such actions are also accompanied by the exploitation of AADTs and tax havens. One should also remember that adoption of this type of tax policy by holding companies causes some countries to suffer substantial budgetary losses because they are consistently avoided by international holding companies engaged in treaty shopping.

Treaty shopping is perceived as a predominantly negative phenomenon, especially when considered from the perspective that such activities harm high-tax countries. Such countries attempt to implement many legal instruments to counter treaty shopping. However, if treaty shopping is to be criticized, one should remember that in addition to illegal techniques that actually do lead to adverse consequences (and have no legal basis), there are legal treaty-shopping techniques. It seems that the nature of treaty shopping is also positive to some extent, considering the existence of the legal techniques. Moreover, one should also consider that possible losses of tax revenue caused by treaty shopping can be compensated for with other types of economic gains, which may have a substantial impact on economic development. Thus, treaty shopping must not be categorized as a phenomenon that has only negative consequences because its macroeconomic aspects exert a substantial influence over some countries' economic development.

Undeniably, treaty shopping is a significant instrument employed by international holding companies adopting a policy of tax optimization. Although it is often considered negative, treaty shopping enjoys widespread popularity among international holding structures.

To recap the issues delineated above, it must be stated that treaty shopping constitutes a significant element of an international holding company's tax-optimization policies; however, methods for countering treaty shopping are also important.

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New Trends in the Development of the Tax System and Their Impact on the Budgetary System of the Czech Republic

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Abstract

Tax system has always reflected changes in society. Real estate taxation was supplemented by labour taxation and later on capital taxation. Currently, the issues of the shared economy and their impact on the area of taxes are being addressed; the European Union is also engaged in a number of tax-related issues, currently the introduction of the so-called digital tax. In addition, it can be expected that the involvement of robots in the economy or the use of new energy sources will raise a number of issues even in relation to taxation. The question is whether developments in society will lead to the creation of new taxes and thus solve the issue of public revenues or will lead to the creation of tax benefits from the existing taxes. It is also a challenge for financial science in the Czech Republic to find ways how to provide sufficient sources to meet the needs of the entire society. The paper will address these issues.

Keywords: Budgetary System; Tax System; Consumption Taxes; Municipality; Local Charges.

JEL Classification: K34.

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1 Introduction: Budgetary Fundamentals and Application of Financial Instruments

High-quality public finance cannot be ordered; any rules can only have an ancillary role as they will set certain limits for budgetary management.[3] The process of reproduction to which the state budget serves is currently not only seen from a narrow point of view of material production, but as an activity aimed at the development of both the intangible needs of the society and its associated relations. Its further changes can be expected with the advent of robotics. Thus, the budgetary process represents an annual concretization of the state policy for the coming year.

Various forms of state revenues and expenditures have gradually been created as a result of changes in social conditions. Governments' needs are nevertheless surprisingly stable in their main features, and it is only up to the choice of the way in which the state will ensure their settlement at the time. In the past, many taxes have had the nature of extraordinary payments, however, over time public budgets have increasingly relied on regular payments in the form of taxes that have been given greater importance. Tax revenues have become a regular resource to meet public needs. In addition to taxes, other charges and payments already considered regular incomes of the public authority have been added even if they were marked otherwise. A regularity element has come to the forefront of classification of budget revenues, and from this concept it was just a step towards a consistent classification of needs where the regularity of occurrence and the level of needs became the basic classification feature. The modern state has gradually increased tasks of state administration, which resulted in public budgets covering new expenditures, namely spending on administrative activities or control. This happened and continues to happen not only at the level of the state but also in other branches of the budgetary system. It is obvious that the costs of public administration – not only at the level of the state, but also at the level of municipalities and regions – will continue to grow together with the increase of the expenditures in the social sphere. It is up to the state

3 It can be said that budgetary law in a broader sense also includes tax law because taxes as revenue of public budgets are contained therein (Karfíková, Boháč, 2015: 36).

to decide whether and to what extent individual budget areas will be supported or to decide to involve more resources of municipalities, regions and the population.[4]

Since the early 1990s, in the Czech Republic there have been political attempts to establish an institutional objective in the economic activity of the state, namely the balanced state budget. From a legislative point of view, the implementation of this objective was proposed in a variety of ways – for example, in 1998, the deputies requested a legal basis for a single sentence: "*The state budget of the Czech Republic is proposed and approved in such a way that, in the given financial year, the state budget expenditures for securing the tasks and covering the needs of the Czech Republic do not exceed the revenues of the state budget.*" No such a proposal has been approved.

As a rule, the government looks to budget issues in such a way that it mainly considers its own solution to be the right path for stabilization. The choice of path is then reflected in the laws that are accepted for this area. Due to the constant growth of needs and thus state expenditures remains unanswered the question of whether development in the society will lead to the creation of new taxes addressing the issue of public budget revenues, or whether the tax incentive path for existing taxes or the search for savings on the expenditure side will be chosen.

2 Budget Responsibility

A step towards ensuring the stability of public budgets in the Czech Republic was the adoption of the Act on Budget Responsibility in 2017. According to the explanatory memorandum to the draft law, it is the main instrument to gradually achieve the sustainability of the Czech Republic's public finances, which requires a strong, consistent, comprehensive and especially stable national fiscal framework. It is a framework defining institutional coverage, fiscal rules and compliance monitoring by an independent National Budget Board, and other measures to strengthen the transparency of public finances and to meet the requirements of EU budgetary frameworks. At the same

4 Support for industry and commerce has long been considered to be the leading state function, which has, moreover, been at the roots of financial science. Cf. the book Veřejné finance (Public finance) of 1927 written by C. F. Bastable.

time, the application of this law should address the discrepancy between the government's responsibility for complying with international obligations under the Treaty on European Union (in particular the provisions of the Protocol No. 12 on the excessive deficit procedure annexed thereto) and the Treaty on the Functioning of the European Union in the field of fiscal discipline on the one hand and instruments of the government on the other hand (Marková, 2015: 287).

Within the current globalization framework, problems of a single state can easily be transferred to another one. In the case of states that are involved in a particular community, it is a necessity for all states to seek common procedures and to set limits to be transposed into domestic legislation, which will allow both the development of individual states and the community as a whole. Within the European Union, member states have their own rules for budgeting. The European Union can only co-ordinate national budgetary policies within the framework of the common rules adopted; in the field of taxation, the uniform approach is only applied to certain taxes; the area of expenditure is not yet subject to regulation. The Czech government has only certain governmental bodies under its direct control, but budgetary policy is implemented by all levels of government in the broadest sense – that is, territorial self-governing units, health insurance companies and other public institutions. The current national framework is therefore based on fiscal targeting, multi-annual spending frameworks and fiscal decentralization. Public budgets, state revenue and expenditure limits are a key element in enforcing interests of the government in any country.

3 Budget Revenues

3.1 Changes in the Tax System and Their Impact on the Budgetary System of the Czech Republic

The system of taxes is based on Act No. 212/1992 Coll., on the System of Taxes, which was repealed by Act No. 353/2003 Coll., on Consumption Taxes, but the tax system established on 1. 1. 1993 recorded several partial changes (Karfíková, 2018: 7–20). Changes in the laws concerning individual taxes were mainly made in connection with the entry of the Czech

Republic to the European Union on 1. 1. 2004 when the need for harmonization of indirect taxes (i.e. value added tax and excise duties) with EU law emerged.

At the initiative of the European Union, changes concerning particularly indirect taxes have therefore been and are still being carried out.[5] Changes in value added tax (VAT) were, among other things, justified by the need to reduce VAT evasion which was at the same time a way how to increase VAT collection.

The basic feature of the legislation – the taxation of consumption when delivered to the final consumer – has been reflected in the whole group of consumption taxes (excise duties). In addition to gas or electricity, the same approach was applied to solid fuels since 1. 1. 2008 with the introduction of tax on solid fuels. A certain feature of the Czech legislation was that the implementation of the tax on solid fuels did not take place by way of an amendment to the Act on Consumption Taxes. The so-called energy taxes (tax on natural gas and some other gases, solid fuel tax and electricity tax) were introduced by a new law: Act No. 261/2007 Coll., on Stabilization of Public Budgets. This law was one of the measures to increase the revenues of the public budgets and a part of the Government Declaration.[6]

A new consumption tax on raw tobacco as a non-harmonized excise duty was introduced in the Czech Republic as of 1. 1. 2015. At present, the adoption of another consumption tax on heated tobacco products is being addressed. This is again a new non-harmonized excise duty. The heated tobacco products that were introduced to the Czech market in the second half of 2017 are products that represent an alternative way of using tobacco through a facility that heats up special tobacco refills. According to the manufacturer's declaration and in line with previous analyses, this should be a less harmful way of using tobacco as there is no direct burning of tobacco. Based

5 E.g. the obligation to introduce a system of gas taxation has emerged from Council Directive 2003/96/EC.

6 As part of this measure, the income tax base for dependent activity under provision (6) of Act No. 586/1992 Coll., on Income Taxes, was extended by social and health care insurance contributions paid by the employer for employees; the so-called super gross wage, which was supposed to be a temporary solution to budget revenues, was introduced.

on the above-mentioned expert analyses, heated tobacco products cannot be classified within the existing categories of tobacco products under the Act on Consumption Taxes and is therefore not subject to taxation.

Other changes in the tax system were implemented in connection with the new Civil Code that came into force on 1. 1. 2014. It is interesting to note that the changes have been adopted in the form of statutory measures of the Senate at the time when the Chamber of Deputies of the Parliament of the Czech Republic was dissolved and its function was taken over by the Senate of the Parliament of the Czech Republic. Thus, a new tax on the acquisition of immovable property that replaced the real estate transfer tax has been adopted. In connection with changes in the field of civil law, there was another change in the tax system, namely the abolition of inheritance tax and gift tax – these taxes have been incorporated into the Act on Income Taxes (Marková, 2016: 331).

The tax system also responded to the new legal regulation of the gaming market. With effect from 1. 1. 2017, the gambling tax was introduced. The law brings different rates for different types of games and also tries to address the issue of online playing. It is also possible to mention the budgetary determination of this tax because the revenue of the tax is divided in most cases between the state budget and municipal budgets (70 % and 30 %); in case of technical games the tax revenue of 35 % comes to the state budget and 65 % to the budget of respective municipalities. The individual municipal budgets are then allocated proportionally according to the number of game positions allowed in the territory. A substantial difference from the general taxation rules is the tax self-assessment, i.e. the assessment of the tax on the basis of submitted tax return or a tax return that was not even submitted. No order for payment is issued and the tax obligation is established automatically. This, however, does not exclude the fact that the tax administrator has the power to issue an adjustment notice (not an order for payment). Positive feature is also that the gambling tax does not include any statutory tax reliefs or exemptions.

The issue of taxation concerning the property settlement with churches and religious societies also relates to tax issues and budget revenues. The Act on Property Settlement with Churches and Religious Societies addresses

the issue of financial settlement between the state and churches and religious societies. Financial settlement is a combination of two institutes – financial compensation and a contribution to support the activities of the churches concerned. Both institutes are not, as stated by law, subject to tax, charge, or other obligatory payment. Entitlement to financial compensation arises from the law (*ex lege*), subject to the condition that the churches and religious societies concerned do not refuse to conclude a settlement agreement. The financial compensation is a lump sum the amount of which represents the value of the original property of registered churches and religious societies, which is not transferred to authorized persons in accordance with the Act on Property Settlement with Churches and Religious Societies because it does not meet the transfer conditions. The financial compensation is fixed by law in a total amount of 59 billion CZK. This amount shall significantly increase as a result of the second year of repayment, i.e. from 2014. The outstanding amount of the financial compensation will be increased depending on inflation so as to preserve the real value of annual instalments. The present draft law provides for the taxation of financial compensation as a possible step towards ensuring that the financial compensation is, as a result, reasonable. With regard to the above-mentioned legislative proposal, the deputies that submitted the bill pointed in particular to the fact that the restitution of ecclesiastical property differs significantly from the restitution legislation that has been implemented so far, especially with regard to the amount of the financial compensation and the method of its determination (valuation of unpaid assets).

3.2 Budgetary possibilities of municipalities

The question is, what options gives the budgetary system as a whole to the revenues and expenditures of lower budgetary entities. Municipality itself cannot introduce taxes or other similar payments, but has certain powers in the construction of tax obligations.[7] Would it be a solution to the

7 Under article 101(3) of the Constitution of the Czech Republic the regional administrative units – communities and regions – are public corporations which may own property and manage their own budget. Their budgets do not form a part of the state budget as the budgets of regions and communities are separate (Marková, Kopecký, Suchánek, 2016: 126).

budgetary situation of municipalities to transfer the revenues of some other taxes or similar payments from the state budget to these components of the budgetary system? Should the municipality's revenue side be supported by the state or should a wider framework be created to meet the public needs?

The structure of expenditures of a particular state or a public corporation (municipalities and regions) is largely determined by past developments, priorities of elected representatives or the economic power of the entity. The size of the municipality may also play its role. If it is a bigger entity, it also has higher budget revenues[8] and may have a more diverse structure of expenditure. The existence of a large number of small entities gives the state authority greater opportunities to decide on the revenue groups that will be assigned to these entities. Expenditure naturally depends on the amount of income or the reserves created in the past (in the form of a surplus of the municipal budget), but the resulting structure of the budget expenditure characterizes to a certain degree the preferences of the population in the given territory. The expenditure side of the state budget must reflect the needs of the state and its population as a whole, both at the level of nationally reimbursed expenditures and in the form of subsidies directed to the budgets of regions and municipalities (Marková, 2016). The answer to the question of whether it can be a solution for the revenue side of municipal budgets to create a legal framework for the introduction of new mandatory payments or whether it is more appropriate to redistribute the yield of existing taxes is not clear.

In general, it is considered appropriate that the revenue of the municipal budget is sufficiently high to allow it a financial self-sufficiency. Revenues should, to a certain extent, also be dependent on municipal activity and should be distributed across the territory to enable public goods to be secured to citizens without greater disparities in structure, quantity and quality between municipalities. At the same time, the provision of budget revenues should not be administratively demanding. And what can be the revenue that can be expected in the future and what will be the resources to meet the public

8 This may not always be the case, but it is usually so when considering the division per capita.

needs? It is clear that such revenue must be based on certain legal principles and rules that are part of the legal order as a whole or, where appropriate, individual legal sectors. Legal principles are the governing ideas of legal regulation and their content is decisive for the content of the legal order as a whole (Tryzna, 2009: 220). Among the basic principles from which the revenue side of territorial budgets derives, the principles (Matoušková, 2000) of financial autonomy, taxation powers, merit, solidarity and stability can be mentioned (Karfíková, 2018: 34).

Financial autonomy occurs when the municipal budget revenues are secured by the applicable law and the exercise of self-government is not restricted by state supervision over management of public funds by municipalities. Taxation power means not limiting the exercise of self-government in the management of public funds. This principle is implemented by surcharges to centrally established taxes or by the possibility to introduce municipal or regional taxes (there is no such option at present in the Czech Republic). The principle of merit means that income remains where it has been created. The use of this principle is denied by the statement that the municipality does not in fact affect the tax yield of the territory by its own activity. Denial of this principle reduces the involvement of local authorities in obtaining additional funds, weakens the link between the incomes and expenditures of the territorial unit and the interest of the public in the municipal budget. Therefore, the rejection of this principle cannot be considered as a benefit to the budgetary management. The principle of solidarity is the opposite of the principle of solidarity, which means that the budget income of entities at the same budgetary level will practically be the same as the municipalities receive income depending on the population. The argument of the supporters of the principle of solidarity comes from the fact that most of the public revenues are directed to securing public goods and exercising delegated powers, which should have the same extent throughout the country. The size of the municipalities in the Czech Republic contributes more to the application of the principle of solidarity than the principle of merit. The principle of stability is fulfilled by making the legislation that concerns the budget and its revenues stable. This principle is not much observed in the Czech Republic as changes in tax laws are

very frequent. From the characteristics of these principles it is obvious that their application to the municipalities' budgetary management has its limits.

All currently applicable taxes are national and mandatory. Municipalities are only given a limited possibility in the case of real estate tax to vary the amount of this tax according to local conditions. The use of a number of coefficients and possibilities of tax exemption provided by this legislation shows that to a certain extent this could be the way of linking the nationally applicable taxes and charges legislation to local conditions. However, it is questionable to which mandatory payments such an adjustment shall be applied. Even with regard to the process of unifying taxation within the EU, it is clear that such an approach is only possible to a very limited extent.

One of the options that could be used is to convert some of the mandatory payments into taxes. This would in particular involve greater differentiation in charges, particularly local ones. Local charges become compulsory payments if a municipality decides to introduce them based on generally binding decree issued by the municipal council within independent competence of the municipality. This creates a situation in which the local charges do not have to be collected in all municipalities (unlike state taxes), they can be territorially differentiated and their scope is limited by the legal definition of their basic construction elements. Municipalities may, by their generally binding decree, soften the legal regulation but not make it stricter as they have to remain within the framework provided by law.

In the case of some local charges, their conversion to national taxes would also be a possible way when supplementing or amending the tax system. This direction can be seen in the effort to convert local charges associated with stay in a particular place and accommodation (use of accommodation facilities) in a single payment. Such a payment is supposed to help municipalities tackle the problem of new trends in the provision of accommodation services within the sector of shared economy. The draft amendment to the Act, however, remains within the framework of the current legislation on local charges. This newly designed local residence charge brings to some extent together two currently applicable local charges: local charge on accommodation capacity and local charge on spa and recreation stay.

4 Conclusion

Implementation of the state's expenditure policy requires sufficient resources. The largest share of government revenue consists of tax revenue. The most important items of the state budget are social security payments, value added tax, consumption taxes and income tax of legal and natural persons. The Supreme Audit Office is constantly focusing on the control of the above taxes, and the results of its audit investigations show that tax administration in the Czech Republic is complex and administratively demanding for both tax administration and taxpayers while pointing to the potential for its simplification and the potential of electronic tax administration. For example, the Office has assessed that the Act on Income Taxes which has been amended more than 130 times since its adoption, is incomprehensible, complicated and contains a number of exceptions that are complicating tax administration, increasing administrative burdens and not contributing to the efficiency of tax collection. Ministry of Finance agreed with these findings and concluded that the current income tax system is confusing and complex. An entirely new Income Tax Act is being prepared to resist the negative effects of the frequent introduction of exemptions.

The situation is similar at the level of municipalities, which, unlike the state, cannot influence what mandatory payments will exist, but can obtain from the state a possibility of responding to local conditions within the framework of a national regulation. The possibility of influencing budget revenues is rather limited at the level of municipalities. It is worth considering to adjust the current system of local charges and create some space for greater municipal activity in obtaining budget revenues. If the inspiration of legislators to design a new tax payment in the form of a municipal tax was based on the Act on Real Estate Taxes, the municipalities would have more options to influence their own budgets. The possibility to influence the amount of tax payments or to directly benefit from tax payments would lead to greater transparency of payments. However, it is open to debate whether the conversion of local charges to tax payments would be acceptable to municipalities that could lose the possibility of deciding on the introduction of these payments. This might be considered an interference

withřtheir separate competences although on the other hand, their ability to influence the level of income is maintained.

We believe that the time has come for the tax system to undergo substantial changes. It is a challenge for financial science to look for and find paths to provide sufficient income to meet the needs of the entire society. Theoreticians should help with this legislative work.

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Airbnb Taxation

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Abstract

There is no discussion that the Airbnb phenomenon causes many problems especially in traditional tourist destinations: lack of long-term rents in the city centres, higher prices of houses and apartments, higher rents, discomfort for locals (increased noise, reduced privacy, etc.) which means that people are moving from the city centres to the suburbs. There are calls for stricter Airbnb regulation. The main aim of this paper is the verification of the hypothesis that tax regulation de lege lata is adequate for fair tax payments of the Airbnb entrepreneurs. Using the method of critical analyses, the areas of personal income tax, tourist taxes and selected tax administration issues were investigated. Synthesizing the gained knowledge, concerning income taxation, the tax office should investigate what type of contract de facto is concluded and what partial tax base is to be used. Regarding tourist taxes, the principle of fair competition is not respected and it is necessary to replace two existing local tourist charges for one. Dealing with the tax administration issues, the existing regulation is adequate and the cooperation between the Airbnb and tax administration is conditio sine qua non for fair tax administration. We do believe that the best Airbnb regulation is the fair Airbnb taxation.

Keywords: Airbnb; Tax; Personal Income Tax; Tourist Tax; Tax Administration.

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1 Introduction

The industrial revolution 4.0 allows completely new technologies for business and society. We can see many innovative trends connected with the digitalization leading to the possibilities in private life, business, and state administration. Thanks to our mobile phones, we can use shared technologies and shared services (e.g. car-sharing, bicycle-sharing, coffee cup-sharing), in many cities the traditional taxi service is replaced by Uber and traditional hotel accommodation is substituted by the Airbnb. Originally the sharing economy meant growing out of the open-source community to refer to peer-to-peer based sharing of access to goods and services (Hamari, Sjöklint, Ukkonen, 2016) to optimize of resources through the mutualisation of excess capacity in goods and services (Sundararajan, 2013). However, this definition has been changed. The sharing economy now covers any sales transactions that are done via online market places, incl. business to business transactions and indirect transactions through the mediator.

The same changes happened in the area of accommodation. Airbnb is the perfect example. Few years before, you would probably never guess that letting strangers into your own home, going into other strangers' houses and trusting them with your belongings and personal safety, or that even going into strangers car on daily basis would be considered as something completely normal and nothing to be concerned about. Especially if you were parent, you would probably couldn't believe that now you will be actually encouraging your children to go into strangers' car, because you consider ordering an Uber a safer option then letting them drive by themselves in big cities. The power of shared economy in digital world has grown very quickly and the numbers for the sake of eliminating many negative impacts of these phenomenon's as mentioned above (for example influencing apartment prices in city centres as people who consider buying an apartment as an investment with the primary intention to use it for tourist coming via Airbnb are willing to pay more money for them) or to protect the principle of fair competition (at the market with short-term accommodation) cannot be ignored and the proper taxation is the right tool to use to control the situation more.

Airbnb ("Air Bed and Breakfast") is an online market space (platform) where people can rent out their spare rooms or even whole houses to guests. The company itself does not own any properties that they would offer to rent out, they are just an intermediary between the host (e.g. the owner or the administrator) and the guest and taking percentage of the transactions between them. Precisely, it is 3 % of the income of the host and between 6–12 % from the guests. (Airbnb, 2019).

It is a new way of short-term accommodation. The primary factor of the huge popularity of this start-up which is now valued at more than 10 billion dollars is the financial factor. It creates "win-win" situation for people who want to find short-term place to stay (it could be in locations where hotels would charge significantly more) and for the owner of spare room or house who wants to take advantage of his/hers property for making some income with no long-term obligations that they would have with renting it long-term, and, again, the possible income is definitely higher. Both sides evaluate each other on the peer-review system, so they both are motivated to make the contract run smoothly for the sake of possible future contracts.

As mentioned above, the primary aim of the Airbnb (and similar companies) was to use vacant apartment or house for a short period of time (e.g. when leaving for holiday) for those who need the accommodation at the moment to save fixed expenditures connected with the rented property. However, the Airbnb turned into the real business generating huge profits. Many natural persons and legal entities are investing money buying apartments in tourist destinations with the intention to rent them for short periods of time to tourists. Definitely, it is not illegal nor unethical. On the other hand, there are several obligations connected with such a kind of business, incl. tax obligations. Some legislators argue that it is necessary to react on the new situation and amend existing rules of income taxation. In contrast, the legal norms should be general enough to be able to deal with the innovative solutions. We believe that they are, no matter many persons offering accommodation by the Airbnb disagree and pay no taxes from this income.

The main aim of this paper is the verification of the hypothesis that tax regulation *de lege lata* is adequate for fair tax payments of the Airbnb entrepreneurs. To confirm or disprove the hypothesis, it will be necessary

to describe the Airbnb and the ways how this business works. As corporate income tax covers all incomes of legal entities and there are no special circumstances for the Airbnb incomes, we will focus on the analyses of natural persons and the personal income tax. Additionally, we will deal with local tourist taxes/charges. These terms are used as synonyms in this contribution, although the tax theory defines the tax as an obligatory amount defined by an act with a laid down rate which is more or less regularly collected from the incomes of economic subjects to the public budgets on the irrecoverable principle and without any consideration, while the fee (or the charge) is irregular and collected by the State or other public corporations for certain legal acts. (Mrkývka, 2008; 6; Gliniecka, 2016). I am the advocate of the correct terminology and I support the differences between taxes and charges in the legislative. However, there is no difference between "tourist tax" and "tourist charge", as it is very difficult to decide whether there is any direct consideration from the municipality for tourist (e.g. direction indicators, maps, and as well clean public places, repaired monuments, etc.). As most of the problems connected with the Airbnb taxation are connected with the lack of information of the tax administrators (tax offices), in the contribution we have to include related tax administration issues. In these parts, we use method of critical analyses, too. Synthesizing the gained knowledge, we are able to summarize conclusions and present possible *de lege ferenda* regulation.

This research is innovative and original, as there are no books, scientific articles nor conference proceedings contributions dealing with the Airbnb taxation issues in the Czech Republic. The only available material is the Tax Administration's methodology.

2 Personal Income Tax

To analyse how the incomes from the Airbnb are to be taxes, it is necessary to define basic circumstances how the Airbnb incomes are generated. There are three possible partial tax bases to be used: incomes from independent activity, rental (lease) incomes, and other incomes.

2.1 Incomes from Independent Activity

Concerning the Airbnb, there are persons running business in the area of rents and/or accommodation services. The rented property is included in their business property. The partial tax base from independent activity is created by all incomes reduced by the expenses incurred to generate, assure and maintain income specified in Art. 24 of the Income Tax Act (Act no. 586/1992 Sb., as amended). If the taxpayer does not have enough expenses, he may claim lump sum expenses. In case of the Airbnb, the lump sum expenses are 60 % of the income from other industry and trades incl. accommodation service (or 40 % of the business is run without trading license) or 30 % of the income from rents of real estate included in the business property (Radvan, 2017). *De lege lata*, lump sum expenses can be used only if the maximum value of lump sum expenses does not exceed 600 000 CZK in case of incomes from other industry and trades and 300 000 CZK in case of incomes from rents of business property. *De lege ferenda*, these limits are to be doubled.

2.2 Rental Incomes

Regarding the Airbnb, rental incomes are the incomes of non-business persons from the lease of real estate or flats (Radvan, 2010: 14–15). Partial tax base is the difference between the above mentioned incomes and expenses incurred to generate, assure and maintain income specified in Art. 24 of the Income Tax Act. The taxpayer does not often have any expenses at all; for this situation the taxpayer can claim lump sum expenses at 30 % of his income. Lump sum expenses can be used only if the maximum value of lump sum expenses does not exceed 300 000 CZK, however, this amount will be doubled this year.

2.3 Other Incomes

The other incomes include generally occasional activities up to 30 000 CZK per year (Radvan, 2010: 15); in case of the Airbnb occasional incomes from accommodation services. The partial tax base includes the incomes reduced by expenses which can be submitted as having been incurred in order to generate such income.

2.4 Independent Activity, Rent, or Other Income?

The crucial issue to be analyzed to subtract the Airbnb into the type of income and adequate partial tax base is the nature of the performed activity. Czech Civil Code (Act no. 89/2012 Sb., as amended) defines the business in its Art. 420 as a gainful activity carried out on its own account and liability in a commercial or similar manner with the intention of doing so on a continuous basis in order to obtain a profit. Providing accommodation is a commercial activity, while rent is excluded from the regulation of commercial activities and regulated in the Civil Code (Art. 2201–2331). The most important difference is the periodicity of the contracts: while in case of rent the contract is long-term (in months or years), in case of commercial activities there are several repeated short-term (in days) contracts with different guests. The other important criteria to be taken into consideration is the service provided for the guests (no service connected with long-term rent vs breakfast, cleaning, linen change, etc. in case of short-term accommodation providers), the purpose of accommodation (providing housing needs vs recreation), routine maintenance and minor repairs (not included for rents), etc. (Ministry of Finance, 2017) Moreover, there are several decisions of the Court of Justice of the European Union dealing with the definition of rent (C-326/99 Goed Wonen, C-409/98 Mirror Group, C-346/95 Blasi, etc.).

The tax office should investigate what type of contract *de facto* is concluded. There are many possibilities how to do that. The easiest one is advertisement screenings, however also witnesses might be interviewed or local investigation could be performed. In most cases, if the accommodation is offered by the Airbnb web pages, it is a business as defined in the Civil Code and an independent activity as defined in the Income Tax Act. However, while information published by the Ministry of Finance (2017) is dealing only with incomes from independent activity and rental incomes, it is necessary to include other incomes, too. If the typical Airbnb service is provided (i.e. it has generally all the characteristics of commercial activity), but only occasionally (i.e. not on a continuous basis), it is the other income. And occasional activities of one taxpayer generating profit up to 30 000 CZK in the calendar year are exempted from taxation.

It should be noted that only taxpayers generating profit from independent activities are the subjects of revenue registry as defined in the Revenue Registry Act (Act no. 112/2016 Sb., as amended) (Radvan, 2018). Such a taxpayer might have other tax obligations in the area of VAT and social and health contributions. For the immovable property tax, the property should be taxed as a structure used for business activities by the higher standard tax rate and related coefficients.

3 Tourist Taxes

The Local Charges Act (Act no. 565/1990 Sb., as amended) provides for the power of municipalities to assess local charges by means of issuing their generally binding ordinances (bylaws). Such ordinances must specify the conditions for levying, the charge rate, the charge maturity and possible exemptions, if any. The ordinances may not exceed the limits defined by the Act (e.g. the absolute charge rate and the types of charges permitted). Presently, the municipalities in the Czech Republic have the opportunity to levy two tourist charges: charge for spa and recreation stay and charge for housing capacity (Radvan, Mrkývka, Schweigl, 2018: 903–904).

Both charges can be collected only during a certain part of the year or only in certain part of the municipality. They have a lot of similarities; that is why *de lege ferenda* there should be only one tourist charge in the Czech Republic, primarily based on the existing structural components of the charge for spa and recreation stay.

3.1 Charge for Spa and Recreation Stay

The taxpayer of the charge for spa and recreation stay is natural person who temporarily stays in spas or other recreation centers because of treatment or recreation and pays for the accommodation. There is a group of persons not liable to charge (blind people, the handicapped, young people (under 18) and old people (over 70) and people receiving children allowance). The taxpayers pay the charge together with the price for accommodation and the owner of the hotel, house, flat or apartment (quartermaster – the payor – natural or legal person) must send the charge to the municipality.

The charge can be collected by all municipalities: if there is no spa (as stated in the government decree) in the municipality, it becomes a recreation center just because the municipality imposes the charge for spa and recreation stay. The guest should tell the quartermaster and prove the purpose of stay: only if s/he stays because of other reason than treatment or recreation, s/he is not liable to charge. However, if the reason of stay is unknown to the quartermaster, the fee should be charged. The reason of stay should be recorded in the registration book with the information about the guest (name, surname, address, number of identity card/passport, dates of arrival and departure) kept by the quartermaster for six years after the last record in the book. The registration book might be a good instrument to control the charge duties, especially if it is kept electronically. The charge rate can run to 15 CZK for a person per day. In fact per night, because the first day (the day of arrival) is free of charge. *De lege ferenda* the charge rate should be higher – up to 50 CZK. There is a possibility of lump sum charge per week, month or even a whole year; this lump sum charge must not be higher than 15 CZK for one day.

3.2 Charge for Housing Capacity

The housing capacity charge can be levied in municipalities and in cities at facilities intended for temporary accommodation of guests where the temporary accommodated guests are obliged to pay for accommodation with the exception for facilities for students and pupils like student hostels, dormitories and campuses, hospitals and spa facilities (if they do not run like hotels), and facilities for social and charitable purposes. The taxpayer is the natural or legal person – the quartermaster, usually the owner or the tenant of the facility. But of course the charge will be included in the price of accommodation; in fact there is no difference between housing capacity charge and charge for spa and recreation stay. The quartermaster must keep the registration book with the information about his guests and length of stay for six years after the last record in the book. With the exemption of the purpose of stay, the information is the same as in the case of registration book for spa and recreation stay charge. That is why usually there is just one registration book for both charges. The charge is paid for every used

bed. The charge rate is 6 CZK for a bed per night or there is also a possibility to negotiate a lump sum charge per year.

3.3 Charges for Airbnb

Concerning the Airbnb (no matter what is the partial income tax base), only the charge for spa and recreation stay is applicable, as all the conditions set by the Act are fulfilled. The Airbnb provider as a payor should keep the registration book, should ask for the reason of stay and collect the charge from the guest liable to tax, and should send collected amount to the tax administrator – municipal office. The charge for housing capacity is not applicable for the Airbnb, as typical houses, flats and apartments are not the facilities intended for temporary accommodation of guests. This is, in our opinion, in contrast with the principle of fair competition, as there is one market of temporary accommodation including the Airbnb facilities and traditional hotels, hostels, etc.

4 Selected Tax Administration Issues

Only in Prague, there were 26 172 registered offers of the Airbnb accommodation since 2013 and 12 531 in the last year (2 523 apartments, 9 717 houses and 291 unspecified). 6 189 of them are active, i.e. the stays are available for more than 60 days in one year. The average occupancy is 42,6 % (and almost 60 % among the active offers). 70 % of quartermasters are offering only 1 apartment or house; oppositely, 2 % of them have more than 11 offers of accommodation. The average price for one night is 1 628 CZK (1 818 CZK for house and 827 CZK for the apartment). Altogether, all guests stayed for 1 349 329 nights in Prague using the Airbnb between November 2017 and October 2018. (blahobyty.cz, 2018)

From the above mentioned statistics published by a private person it is obvious that the quartermaster relaying on the fact that the tax administrators (tax offices and municipal offices) are not able to get the information about the Airbnb are wrong. And the tax administration has definitely more tools to get the information about the persons offering accommodation and their incomes. The Tax Code (Act no. 280/2009 Sb., as amended) sets several

possible means of proof to detect persons offering accommodation using the Airbnb and the revenues they get. The easiest evidence is the witnesses' interview; as witnesses, usually the neighbors are interviewed. However, such an evidence is time consuming and not always effective, especially if most of the apartments in one house are rented. The other possibility is the local investigation. The negatives are pretty much the same: it takes a lot of time, very often the whole house is locked for anybody else but the guests, etc. The registration book for the tourist charges seems to a be a good tool, however, in reality, most of the quartermasters no not keep this evidence, in spite of the risk of fine, This fine can be imposed up to the amount of 500 000 CZK.

The quartermasters are aware that the above mentioned means of proof are usable only if the tax administrator has any guess that the house or the apartment is rented. Then, what is the primal evidence for the tax administrator to get the information about the Airbnb? In the individual cases, the advertisement screenings (general, or specific on the Airbnb web page) are used. However, this approach is time consuming and not very effective. The ideal method is regulated by the Art. 57(1) of the Tax Code stating that on the request of the tax administrator every person getting the data necessary for tax administration must provide this information to the tax administrator. The Airbnb, Inc. as a business company no doubts fulfills this definition and since 2018 cooperate with the Czech tax offices (Veselíková, 2018). This source of information is the primal one to find out who the person generating profit from the Airbnb is and what the revenues are. If there are any doubts, all the above mentioned means of proof are available for the tax office.

From the perspectives of municipal offices as tourist charges administrators, they have absolutely the same tools as the tax office administrating income taxes and VAT. However, the easier way now is to get the information from the tax office directly; Art. 52(5) of the Tax Code states that such an exchange of information between two tax administrators does not mean the breach of the principle of secrecy.

5 Conclusion

The hypothesis of this contribution that tax regulation *de lege lata* is adequate for fair tax payments of the Airbnb entrepreneurs was generally confirmed, however, there are still some minor issues to be solved.

Concerning income taxation, the tax office should investigate what type of contract *de facto* is concluded and what partial tax base is to be used (incomes from independent activity, rental incomes, or other incomes). The original idea of the Airbnb (usage of vacant apartment or house for a short period of time e.g. when leaving for holiday for those who need the accommodation at the moment to save fixed expenditures connected with the rented property) is tax-free up to the income of 30 000 CZK per year, while the "business Airbnb" is taxed in the same way as any other business activity. There is no need to amend existing legal regulation because of the Airbnb specifics.

Regarding tourist taxes, *de lege lata* only the charge for spa and recreation stay is applicable, while the charge for housing capacity is not, as typical houses, flats and apartments are not the facilities intended for temporary accommodation of guests. This is in contrast with the principle of fair competition, as there is one market of temporary accommodation including the Airbnb facilities and traditional hotels, hostels, etc. As the revenues from the tourist charges are significant (in Prague, the revenue from the Airbnb only is presumed to be 48 960 000 CZK (blahobyty.cz, 2018)), it is necessary to amend the legal regulation. The first step should be to replace two existing local tourist charges for one. The Ministry of Finance has prepared a draft currently discussed in the Parliament introducing the charge on stay (House of Deputies of the Parliament of the Czech Republic, 2018). The taxpayer is the person not registered in the municipality staying in the accommodation no longer than 60 days. The purpose of stay is not taken into account, however, there is the list of exemptions (handicapped persons, children up to 18 years, person over 65 years, persons staying in the hospital, students at the dormitories, etc.). The municipalities have right to set additional exemptions in the generally binding ordinance (e.g. for workers). The tax rate should be at maximum 21 CZK per night (i.e. the same as the sum

of contemporary charges), however in 2021 it should be increased up to 50 CZK. The charge should be collected by the payor. The payor's duty to run the registration book remains. In our opinion the presented amendment is useful and solves a lot of problems. In the Parliament, one can expect discussions especially about the maximum charge rate and the payor: it might be useful to define the internet platform (Airbnb, Flipkey, HomeAway, House Trip, Vacation Rentals, etc.) as the payor especially for the occasional rents offered by non-businessmen.

Dealing with the tax administration issues connected with the Airbnb, the existing regulation is adequate, especially if the Airbnb, Inc. cooperates with the tax administrators providing the data necessary for tax administration, i.e. the list of quartermasters and rented property and their revenues.

There is no discussion that the Airbnb causes many problems especially in traditional tourist destinations: lack of long-term rents in the city centres, higher prices of houses and apartments, higher rents, discomfort for locals (increased noise, reduced privacy, etc.) what means that people are moving from the city centres to suburbs. There are calls for stricter Airbnb regulation. However, we do believe that the best Airbnb regulation is the fair Airbnb taxation.

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Application of Customs and Fiscal Audit Provisions. Selected Problems

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Abstract

The provisions regarding tax compliance have undergone some modifications over the past years. The basic assumption of subsequent amendments was the desire to provide the tax administration with effective legal instruments to ensure effective compliance with statutory obligations in the field of tax settlement audits. Such objectives were also reflected with regard to changes related to the new shape of the tax administration and the introduction of the so-called a tough audit procedure, i.e. customs and fiscal audit, which are aimed at enhancing the efficiency of tax administration operations. Two years of experience related to the application of these provisions allow identifying certain doubts which emerged, and an analysis of recent changes effected in the field of audit procedures invites to make several comments on how the legislator coped with them. The aim of the study is not a comprehensive analysis of the law in the field of customs and fiscal audit due to its fairly wide complexity, nevertheless, the considerations will be limited to selected regulations of relevance in the area of tax law and the revealed doubts related to the audit of taxpayers' reliability concerning their compliance with public law obligations.

Keywords: Tax; Law; Hard Control Procedure; Customs and Tax Control.

JEL Classification: K34; E62.

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1 Introduction

The reform of the fiscal administration (Act on the National Fiscal Administration) and the Provisions implementing the Act on the National Fiscal Administration implemented a new type of control in the area of the tax law, i.e. a customs and fiscal audit. Within a framework of a single procedure provided for in Section V of the Act of 16 November 2016 on the National Fiscal Administration (hereinafter referred to as u.k.a.s.), the following shall be conducted: an audit related to compliance with the tax law, a customs audit and an excise goods audit (previously conducted within the framework of a special tax supervision). How mentioned Cyman (2018), customs establish a specific field of relations.

The implementation of that procedure pursues the legislator's intention to harmonize the procedures applicable to public law settlements audits. However, the scope of a customs and fiscal audit is much broader than merely verification of the observance of the tax law by entities under audit, and the regulations comprise the following: rules of conduct, tasks for the authorities, auditors powers, including operational and intelligence powers, duties of the entities under audit and constitute a syntax of several legal acts (On the basis of the existing regulations, taxpayers are subject to various audit regimes, i.e. both conducted on the basis of the Act of 28 September 1991 on Fiscal Audit (hereinafter referred to as u.k.s.), the Act of 29 August 1997 Tax Ordinance (hereinafter referred to as o.p.) as well as an audit conducted by customs authorities.), with their further extension to certain tasks not yet discharged by the tax authorities, in particular in the area of combating economic crime. Within the framework of a customs and fiscal audit only, governed by the provisions of Section V, we can observe differences which stem from the specific nature of scope of the audit. Clearly, the differences are related to the customs and fiscal audit of the observance of the tax law. Immediately upon the enactment of those provisions, several areas were highlighted in which practical doubts might arise, drawing attention to the need to remove certain debatable issues by the legislator (Strzelec D., et al: Tax law compliance audit, Warsaw 2017). It is worth emphasizing that that act, although it has been in force for less than two years, has been amended in the area of interest a number of times,

and quite significant modifications have been brought about by the latest amendment which removed some of the doubts raised (Act of 9 November 2018 amending the u.k.a.s and some other acts).

2 The subjective and objective scope of a customs and fiscal audit in the area of tax law

First and foremost, from the point of view of the legislator's assumptions, a question regarding the actual use of customs and fiscal s in the field of tax law seems legitimate. In the explanatory statement regarding u.k.a.s., it has been indicated that a customs and fiscal audit is intended to be a so-called tough procedure that will only apply to extremely serious prohibited acts, e.g. organized criminal groups, whereas in other cases tax audits will proceed to be conducted as they have been so far pursuant to the provisions of o.p. Thus, this procedure is aimed at, inter alia, combating the so-called VAT carousel frauds, hence conferring the powers to conduct proceedings in matters regarding offences which can be perpetrated by any offender and which are listed by the law, which are also inextricably linked to fiscal offences and, moreover, extensive powers of operational and intelligence nature (Article 113 et seq. of u.k.a.s.). Taking into account the provision of Article 57 in conjunction with Article 54 u.k.a.s.) we may arrive at the conclusion that the scope of entities with respect to which such an audit may be conducted is unlimited. Nevertheless, one may not lose sight of the fact that, in accordance with the legislator's intentions, presumably, the fundamental function of the head of the customs and tax office will primarily lie in detecting and combating large-scale irregularities, in situations where the size, complexity and severity of the irregularities detected adversely affect the state's financial security system, which should be taken into account while selecting entities for a fiscal audit, in particular, taking into account the provision of Article 58 u.k.a.s. However, taking into consideration the objective scope and a lack of subjective restrictions regarding the possibility of conducting such an audit, it would be reasonable to specify when in the area of tax law observance such an audit may be performed. Hence arises the first of the serious doubts. Namely, whether it is possible to make a demarcation line between fiscal audit and customs and fiscal audit pursuant

to exactly Article 58 u.k.a.s., according to which, while planning an audit, one should take into consideration the risk that irregularities may occur. Probably, only the future will show whether such an audit will be instigated following the conduct of a reliable risk analysis and a selection of entities to be audited, or whether it will also be a consequence of a limited capacity to conduct audit activities in tax offices. Simultaneously, one may consider whether it would be reasonable in the future to prepare a single audit procedure with regard to the observance of the tax law by combining two currently existing audit procedures in line with indicating those provisions which will not apply to the so-called tough audit procedures applied with regard to entities conducting business activities, indicating a high probability of an occurrence of large-scale irregularities as well as the size, complexity and impact affecting the state financial security system (resignation from the institution of prior audit notification, a lack of a territorial jurisdiction, documents security, etc.).

3 Legal regulations applied in customs and fiscal audit

While analysing the provisions regarding customs and fiscal audits, we can see that the new audit procedure has been based on the provisions of the o.p., the u.k.s. and partly the Act of 27 August 2009 on Customs Services hereinafter referred to as u.s.c. Basing the provisions of u.k.a.s. on the current regulations of u.k.s and u.s.c., due to the similar or identical wording of the new legal norms, allows an extensive use of the existing views of legal academics and commentators as well as administrative decisions. At the same time, in the course of customs and fiscal audit, to the extent not regulated in the u.k.a.s., the appropriately indicated provisions of the o.p shall apply accordingly. We may further also notice that in the case of a customs and fiscal audit regarding the observance of the tax law, despite referring to the appropriate application of the provisions of the o.p., there are a few differences with regard to tax audits conducted by heads of tax offices. It mainly relates to the scope of instigating audits on production of a work-related ID card, notification of an audit, principles governing cross audits, completion of an audit and the right granted to correct the tax

return, the possibility of resuming a previously completed audit and individual powers vested in the auditors.

At the same time, it is worth noting that the scope of the reference to the appropriate application of the o.p. since 1 January 2019 has been amended (In the original wording in accordance with Article 94 section 1 to the extent not regulated, for a customs and fiscal audit the provisions of the o.p. applied accordingly: Article 3e, Article 12, Article 102 § 3, Article 135, Article 138, Article 139 § 4, Article 140 § 2, Articles 141–143, Article 165b, Articles 175–177, chapters 1, 2, 3a, 5, 6, 10 and 11, with the exception of Articles 182–185, Article 189 § 3, Article 190 § 1, Article 193 § 6–8, Article 198 and Article 200, chapters 14, 16, 22 and 23 of Section IV, Section VI, with the exception of 282b, Article 282c, Articles 283 § 1–3, Article 284a § 1, Article 284b, Article 285a, Article 286 § 1 and 2, Article 287 § 1 points 1 and 2 and § 3–5, Article 288, Article 290 § 1 and § 2 points 1–7, Article 290b, Article 291, Article 291c and Article 292, and Section VII). Namely, in accordance with Article 94 section 1 to the extent not regulated, for a customs and tax audit the following provisions shall apply accordingly: (1) Article 3e, Article 12, Article 102 § 3, Article 135, Article 138, Article 139 § 4, Article 140 § 2, Articles 141–143, Article 165b, Article 165c, Articles 175–177; (2) chapter IV, chapters 1, 2, 3a, 5, 6, 10, 11, except for Articles 182–185, Article 189 § 3, Article 190 § 1, Article 193 § 6–8, Article 198 and Article 200, and chapters 12, 14, 16, 22 and 23; (3) Article 281, Article 282a, Article 283 § 4 and § 5, Article 284a § 5–6, Article 284ab § 1–3, Article 286 § 3, Article 286a § 1 and § 2, Article 289, Article 290 § 4–6, Article 291a, Article 291d and Section VII – of the o.p. Furthermore, resigning from referring to the relevant application of some provisions of the o.p., which used to be applied in the course of customs and fiscal audits as recently as until the end of 2018, in the provisions of the u.k.a.s., certain new solutions emerged inspired by the provisions of the o.p., and sometimes constituting even their direct transfer to that Act.

The characteristic nature of customs and fiscal audits lies in the fact that the provisions of Chapter 5 of the Act of 2 July 2004 on the freedom of economic activity (hereinafter referred to as: u.s.d.g.) do not apply to customs and fiscal audits. The reason for that situation is the fact that such

audits will be directed at entities with regard to which a suspicion arises that the business activity is conducted in violation of the law. In that respect, two subsequent doubts arise: (1) firstly – is that a cause for concern for taxpayers, with regard to whom this type of audits will potentially be implemented; (2) secondly – does that really mean the decreeing in the explanatory statement of the Act, a unification of audit procedures?

As far as a reply to the first question is concerned, it seems that the solution adopted by the legislator, i.e. that those solutions presumably guaranteed for entrepreneurs and provided for in the u.s.d.g. will not be applied – which itself should not be perceived as a big regression for entities under audit. Unfortunately, such an assessment is adversely affected by the manner in which the provisions of the u.s.d.g. have been applied to date and how that practice has been evaluated by administrative courts (e.g. with regard to the duration of tax audits) (Highest Administrative Court, I GSK 955/09; Highest Administrative Court, I FSK 1045/05; Voivodship Administrative Court in Poznań, II SA/Po 934/11; Highest Administrative Court, I FSK 1045/05; Voivodship Administrative Court, I SA/OI 591/09).

On the other hand, as regards the second question, it should be noted that concerning the new institution provided for in the u.k.a.s., three legal regimes will be established on the basis of the binding legal regulations, allowing assessment of the compliance with the tax law, the application of which will depend on which authority will conduct the audit and which taxpayer is to be verified by that authority, i.e.:

- customs and fiscal audits, undertaken by the head of the customs and tax office, to which the provisions of the u.k.a.s. shall apply, and, by a relevant application, selected provisions of the o.p., and which may be conducted with respect to both entrepreneurs and non-business entities;
- tax audits conducted by the head of the tax office, undertaken with regard to entrepreneurs pursuant to the provisions of the u.s.d.g and the o.p.;
- tax audits conducted by the head of the tax office, under the provisions of the o.p., undertaken with regard to individuals who from the formal and legal perspective do not possess a status of an entrepreneur, thus including individuals who actually perform activities

indicating that a business activity is conducted, however, they are not entered in the business activity register. Such a situation does not constitute a remedy for the existing duality of the audit authorities and the multiplicity of audit procedures conducted in the area of the tax law and criticized in the explanatory statement of the u.k.a.s. Furthermore, it should be made clear that within the framework of a customs and fiscal audit itself, the audit regarding the observance of the tax law provisions also reflects certain specific features (with regard to the instigation, completion as well as the rights the individuals under audit are entitled to with regard to tax return adjustments) with respect to an audit having a different subject, the powers of the authorities conducting the audit.

4 Instigation of customs and fiscal audit

4.1 Resignation from the notification obligation

The instigation of a customs and fiscal audit will not be preceded by notifying the party that such a procedure will be implemented with regard to that party. It results from Article 93 of the u.k.a.s., which stipulates that the provisions of Chapter 5 of the u.s.d.g., which in Article 79 provides for such a general obligation in the case of audits of entrepreneurs, as well as the lack of a cross-reference to a relevant application of the provisions of Article 282b and Article 283c of the o.p. (Article 94, section 1 of the u.k.a.s).

Instigation of an audit in accordance with Article 62 of the u.k.a.s. shall be effected ex officio, pursuant to an authorization to conduct a customs and fiscal audit. The audit commencement date, as at the present time, will be the day of service on the individual to be audited or on a person appointed to represent the said individual or on an authorized representative, a named authorization to conduct such an audit while presenting their professional ID. Under the provisions which remained in force until the end of 2018 in the scope not regulated in the u.k.a.s., the provisions of the o.p. (See. Article 284 § 2 and § 2a of the o.p. in conjunction with Article 94 of the u.k.a.s) were applied with regard to an instigation of an audit. Since 1 January 2019, the structure of cross-references has changed and

the provisions of Article 62 sections 2a-2b and sections 3a-3c have been added to the binding provisions of that Act, which specify the principles regarding the instigation of a customs and fiscal audit without referring to that end to the fiscal audit provisions set forth in the o.p. as it was indicated that as from the legal system perspective, the provision cross-referring to the solutions from the o.p. in the previously binding form (in particular to Article 284 of the o.p.) resulted in some interpretation difficulties and limitations regarding the conduct of audits in the absence of the taxpayer or their representative.

Since 1 January 2019, if the entity under audit is a legal person or an organizational unit without legal personality, the authorization is served on a board member, a partner or another person authorized to represent the person under audit or to conduct their affairs, or a person authorized to obtain correspondence (2a.). On the other hand, when a plant belonging to a foreign entity is audited, an authorization is served on the person who actually manages, supervises or represents the given business activity (2b.). In the absence of an individual to be audited, their representative or a person authorized to collect correspondence, a customs and fiscal audit may be instigated upon production of the professional ID to an employee of the individual to be audited who may be considered a person referred to in Article 97 of the Polish Civil Code, or in the presence of a witness called, who should be a public official who is not an employee of the fiscal administration chamber or an officer (3a). In cases where the person representing the entity to be audited is absent at the time of the instigation of the audit, the authorization to conduct the customs and fiscal audit shall be served on the individual to be audited without undue delay (3b). Simultaneously, by resigning from the relevant application of Article 284 of the o.p., there is no restriction in that respect to undertake audit activities immediately following the instigation of the proceedings, even if the entity under audit avoids accepting the authorization to conduct the audit.

4.2 Audit instigation on professional ID card

The provisions of the u.k.a.s. provide also for the possibility to instigate an audit based on a professional ID card in the event of a suspicion that

the provisions are not observed and factual circumstances justify an immediate audit (Article 62(3) of the u.k.a.s.) In this respect, two important issues should be taken into account. First of all, the conditions provided for by the provisions to instigate an audit upon production of professional ID cards seem to be wider than the corresponding provisions justifying the instigation of a tax audit upon production of professional ID cards stipulated by the provisions of the o.p. (under Article 284a § 1 of the o.p., a tax audit may be instigated upon production of a professional identity card to an auditee, when the audit activities are necessary to prevent a commission of a fiscal offence or a minor fiscal offence or to secure evidence of its commission). The fairly enigmatic premise of the facts in favour of an immediate audit may become a source of conflicts with the entities under audit, in particular with regard to the manner the auditors construe that concept. Secondly, if a customs and fiscal audit is instigated upon a production of professional ID cards in connection with the cross-reference, binding until the end of 2018, to the relevant application of the provisions of Section VI of the o.p., i.e. Article 284a § 2 and § 3, the auditor was obliged to serve an authorisation to conduct the audit without unnecessary delay, but no later than 3 working days of the date of the instigation of the audit. In the event of non-compliance with that obligation, the documents concerning the audit activities did not constitute evidence in the tax proceedings. These requirements have been abandoned as of 1 January 2019, indicating merely in the provisions of the u.k.a.s. the obligation to serve the authorization on the entity to be audited without unnecessary delay.

5 Adjustment of the tax return following the instigation of an audit

Resignation from the obligation to provide notification of a planned audit does not mean that the individual to be audited will be deprived of the right to make an adjustment, the option which is stipulated in the provisions of the o.p. with regard to a notification of a planned tax audit. In the course of a customs and fiscal audit, with respect to verifying the observance of the tax law, the audited individual shall be entitled to adjust the tax return to the extent covered by that audit within 14 days of the date of the service

of an authorization. Any adjustment of a tax return submitted after that date and before the completion of the customs and fiscal audit, shall not produce any legal effects (Article 62(4) of the u.k.a.s.). In practice, that solution after the provisions of the u.k.a.s. had came into force, gave rise to certain doubts. Those doubts concerned the determination whether submission of such an adjustment made sense while the tax authority was still obliged to continue the audit, and at the same time there was a problem regarding the scope of the customs and fiscal audit, if the audited individual filed a tax return adjustment in accordance with the expectations of the tax authority within 14 days of the commencement of the said audit.

The head of the customs and fiscal office, pursuant to the provisions in force until the end of 2018, following the instigation of the audit, was obliged to complete it and to issue the results of the audit, the head was not allowed to withdraw from the audit activities. Due to the latest amendment, that situation has changed since 1 January 2019 and the doubts previously reported have been removed following the addition in Article 62 the following provisions: (4a-4b). Pursuant to these provisions, the head of the tax office, having jurisdiction over the audited individual, shall notify immediately the head of the customs and tax office conducting the customs and fiscal audit of the submitted tax return adjustment. If the head of the customs and tax office has accepted a tax return adjustment submitted by the auditee, the auditee shall be served with a notification on the acceptance of tax return adjustment. The notification of an acceptance of the tax return correction shall finish the customs and fiscal audit and no audit results shall be drafted.

6 Auditors powers

Within the framework of a customs and fiscal audit, the authorities were granted many powers, listed in detail in Article 64 of the u.k.a.s. Their catalogue is quite extensive due to the necessity to equip the auditors with instruments relevant for the scope of their operations, as well as the unification procedure of the u.k.a.s., hitherto implemented by the customs, fiscal and tax administration. The majority of those powers, applied during the tax law compliance audit are identical with the catalogue stipulated in Article 286 of the o.p. At this point, it is worth paying attention to three

of those selected powers, as since the moment those provisions became binding, certain misunderstandings have arisen.

6.1 The right to request documents for other settlement periods

The provisions vest in the auditors the right to request from the auditees documents, that right applies to any and all documents regarding the subject of the audit, including a time period other than the period covered by the audit, if the period of their storage provided for in separate provisions has not yet expired (Article 64(3) of the u.k.a.s.).

In practice, in the light of this provision, a significant doubt may arise, namely: does it actually vest in the auditors the unrestricted power to verify documents of the auditee for time periods not covered by the given audit? Obviously, it seems that this power does not constitute a consent to verify, in the course of an audit for a given settlement period, also settlement periods not covered by the subject of the audit. This provision authorizes solely to request documents for other settlement periods to the extent necessary to verify the facts which occurred during such periods as long as they affect the settlement periods under the audit (e.g. loss settlement, VAT excess, amortization write-offs). Support for such arguments can be found, in particular, in the provisions concerning the grounds for conducting an audit. Namely, in accordance with Article 62(8) of the u.k.a.s., an authorization to conduct an audit should specify the scope of the customs and fiscal audit as well as the expected date of its completion. Auditors are authorized, on the basis of that authorization, to act solely within the scope indicated therein, and any audit findings outside its scope will result in ineffectiveness of the audit activities conducted. The amendment related to the cross-reference to the provisions of the o.p. made as of 1 January 2019 in Article 94(1) of the u.k.a.s. did not exclude the relevant cross-reference to Article 283 § 5 of the o.p. Thus, the possibility to request documents concerning the period other that the period covered by the audit is admissible in so far as they regard operations from which the taxpayer has derived certain legal effects in the period under the audit.

6.2 The right to cross-check

In the course of a customs and fiscal audit, the auditors have the right to conduct a cross-checking (Article 79 of the u.k.a.s.). The head of the customs and tax office may request that the contractors of the auditee grant access to the documents related to the delivery of goods or services (Article 79(1) point 1 of the u.k.a.s.) and that they submit, by means of electronic communication or on an IT data carrier, an extract from fiscal books and accounting documents recorded in an electronic form if the taxpayer's contractor keeps fiscal books by means of computer programmes (Article 79(1) point 2 of the u.k.a.s.), similarly as in the provisions of the o.p. (See Article 274c of the o.p.). On the other hand, with regard to the remaining powers which were granted in the course of a customs and fiscal audit, we can, however, observe certain differences from the principles governing the conduct of those activities provided for in the o.p

Namely, the authorities may also request explanations related to the delivery of goods or services to the extent covered by customs and tax control (Article 79(1) point 3 of the u.k.a.s.). The last of the powers granted is partly connected with certain problems which have occurred in that area on the basis of the existing provisions of the o.p. Namely, we could observe attempts to informally interview contractors, without observing the course of action provided for a witness interview. Quite frequently in such situations, the authorities prepared from such an activity not an interview report, but a document which contained the contractor's explanations, although *de facto* its analysis would give grounds to accept that what we had was a surrogate of an interview of that individual without informing the auditee thereof. It so happened that, in view of allegations against such actions and claims that such practice constituted a circumvention of the provisions which enabled the party to actively participate in the proceedings, the tax administration claimed that they were spontaneous utterances of the contractor made on the contractor's initiative, although the manner in which they were presented in the report might suggest that those were rather replies given to the questions formulated by the authorities. One may be inclined to draw such conclusions first of all from the practice in which contractors are summoned to appear in person with documents at the head office

of the auditors, which may at the same time be connected with the intention to obtain information from them as from human sources of evidence. Subsequently, a question arose whether the contractor's explanations submitted in that regard, which would be aimed at replacing his testimony, which he ought to give in the capacity of a witness, might constitute evidence in the given case?

It was indicated in the judicial decisions that the authorities did not have the right to formally interview an entrepreneur as a witness in that manner, but they could insert his statements in the report; however, they shall not be perceived as witness interview evidence (Highest Administrative Court, I FSK 546/11), whereas in another judgment, the court, also on the grounds of legitimate observations – underlining in the correct manner that these activities are of a limited scope, they may in particular regard documentation, and the authorities may not demand, for example, the submission of explanations by a contractor – concluded that if the contractor talked about issues related to the activities, the authorities should include those utterances in the report. In the court's opinion, reports from verification activities conducted at contractors' places did not provide grounds to agree with the opinion that in the course of those activities, the auditees were interviewed, in which interviews the party was not granted the right to participate. The explanations included in the report, in so far as the authorities of the first instance refer to them, concerned basically the documentation kept by those entities, in particular the method of documenting transactions (Voivodship Administrative Court in Białystok, I SA / Bk 216/08). Highest Administrative Court also found similarly, refusing, however, to adopt a resolution in that regard (Highest Administrative Court, II FPS). Implementing of Article 79(1) point 3 of the u.k.a.s. which stipulates the possibility to request explanations from contractors appears to legitimize exactly such practice applied sometimes so far.

Furthermore, in Article 79(2) of the u.k.a.s. it has been clarified from the subject-matter perspective, who is to be an auditor's contractor, recognizing as such that all entities conducting business activity, involved in the delivery of the same goods or services, being both suppliers and buyers participating indirectly or directly in the delivery of goods or services. At the same

time, due to an amendment to that provision since 1 January 2019, the definition of an auditee's contractor has been extended to include also a carrier as well as all entities conducting business activity in the period covered by the customs and fiscal audit participating in storing, repacking, reloading, forwarding the same commodity, operating both on behalf of suppliers and buyers who participate directly or indirectly in the delivery of goods.

6.3 The right to assess the tax base

It is worth noting that in the original version of the u.k.a.s there was no cross-reference to the appropriate application in the course of a customs and fiscal audit of the mechanism of assessing in the absence of books (Article 23 of the o.p.). That produced certain doubts as to whether in the absence of books at the stage of that audit, it is possible to assess the tax base. A lack of appropriate provision in the Act meant that if a customs and fiscal audit was conducted at a taxpayer's place, who does not have fiscal books, or if such books were found to be unreliable, where there was a need to assess the tax base, it was impossible to determine the extent of depletion and thus the taxpayer who obtained the results of the audit had a limited right to submit an adjusted tax return. On the other hand, if the adjustment was submitted after the results of the customs and fiscal audit, the authorities had difficulty verifying its correctness. Therefore, as of 1 January 2019, Article 79a was added which stipulates that in the course of a customs and fiscal audit, the head of the customs and tax office may assess the tax base on the basis of separate provisions, i.e. Article 23 of the o.p.

6.4 Fiscal books auditing procedure

Simultaneously, it should be noted that in the course of a customs and fiscal audit, the legislator addressed the procedure of auditing books in a fairly peculiar manner. Namely, the findings in that respect may be included in the results of the audit without the obligation to prepare a separate audit report referred to in Article 193 § 6 (Article 290 § 5). This is due to the fact that in the course of that audit in accordance with Article 94(1) of the u.k.a.s., Article 193 § 6–8 of the o.p. shall not be applied, whereas that Article provides for a procedure for challenging the special evidential

value of books, giving the taxpayer the right to submit reservations in that regard (During a customs and fiscal audit, Article 94(1) refers to the application of Article 290 § 5, under which an audit report may also contain findings concerning books auditing to the extent provided for in Article 193. In such a case, a separate report concerning books auditing and referred to in Article 193 § 6 shall not be prepared). However, in the course of a customs and fiscal audit, in accordance with Article 82(1) point 6 in conjunction with (2) of the KAS, a report shall be prepared from the audit of documents and records, the report shall be read and the auditee is not entitled to raise any objections in that respect. It is worth emphasizing that currently, in the event of a service of the results of an audit, which may contain findings regarding books auditing, the auditee's right to submit objections has been provided for.

7 Completion of customs and fiscal audit in respect of compliance with the tax law

7.1 The manner of completing the audit

The most serious changes in the principles governing a customs and fiscal audit in the field of the tax law are related to the manner of its completion and rights to which an auditee is entitled. Namely, upon completion of audit activities performed in the course of a customs and fiscal audit, conducted with regard to compliance with the tax law, the results of control are served (Nevertheless, there are exceptions of situations where no audit results are drawn up, among others, (a) during an audit to verify compliance with the tax law with regard to turnover registration by means of cash register devices; (b) during an audit to verify compliance with the tax law with regard to production, shifting and consumption of excise goods – however, as long as no irregularities were found (Article 82(5) of the u.k.s.) and the audit concludes when that document is served on the auditee (Article 82(1) of the u.k.a.s.). The results include, inter alia, information regarding irregularities found or a lack of irregularities. Due to the results service, in a situation when the authorities indicated irregularities in the taxpayer's settlements, the auditee – unlike in the course of a tax audit conducted by the head

of the tax office – was not entitled to submit objections but the auditee was entitled to decide whether the auditee would exercise their right to adjust the tax return, to the extent covered by the audit, whether the auditee would seek their rights, but under another procedure, namely, tax proceedings. In the event of detecting irregularities in the course of the audit, if the auditee failed to submit a tax return adjustment or the authorities did not accept the tax return adjustment submitted, or the authorities accepted the tax return adjustment submitted and there are premises to determine additional liability related to goods and services tax or there are grounds to determine a tax amount payable pursuant to Article 108 of the Act of 11 March 2004 on Value Added Tax hereinafter referred to as u.p.t.u., the audit is transformed into tax proceedings (Article 83(1) of the u.k.a.s.). The transformation itself is effected on the day of service of the transformation decision against which an appeal shall not apply.

7.2 The deadline for issuing a decision regarding an adjustment submitted

One of two of potential decisions of the auditing authorities is possible with regard to an adjustment submitted by the taxpayer. Namely, when the authorities accept the adjustment, i.e. it contains information that irregularities have been found as a result of an audit, the authorities serve a notification of acceptance of the tax return adjustment on the auditee (Article 83(2) of the u.k.a.s.). However, if the authorities have not accepted the tax return adjustment since it, for instance, rectifies solely a part of the irregularities detected in the course of the audit, the authorities issue and serve on the party a decision to transfer the audit into tax proceedings (Article 83(1) of the u.k.a.s.). Thus, it means that only by submitting an adjustment which rectifies all the irregularities indicated in the results of the audit, shall the auditee avoid a transformation of the audit into tax proceedings. Yet, this does not apply to situations where an additional tax liability may be imposed or there are premises to establish a liability payable under Article 108 of the u.p.t.u. In such a situation, notifications of acceptance of a tax return adjustment are included in the decision to transfer the customs and fiscal audit into tax proceedings.

The provisions of the u.k.a.s. do not specify the time limit for issuing the aforementioned decision, nevertheless, it does not mean that the authorities are not restricted in any way in that respect. Namely, in connection with the appropriate application of ("Appropriate" application of a provision may consist in its application directly or with some modifications – justified by the differences of the "pulled up" status for the wording of provision applied (Highest Court in the Resolution of 6 December 2000, III CZP 41/00) Article 165b of the o.p. in connection with Article 94 of the u.k.a.s., it should be assumed that if the audit reveals irregularities regarding the compliance of the auditee with the obligations arising from the provisions of the tax law and a failure to submit a tax return on the part of the taxpayer or the taxpayer's failure to adjust the tax return fully rectifying the irregularities revealed, the authorities issue a decision no later than 6 months of the date of completion of the audit, i.e., the service of the results of the audit.

7.3 The effectiveness of a power of attorney submitted in an audit also in the course of the proceedings

In practice, another doubt was revealed related to the completion of a customs and fiscal audit and its subsequent transformation into tax proceedings. Namely, on whom the decision on the transformation of the audit into tax proceedings should be served – on an auditee or on a representative – if at the audit stage the auditee was represented by a representative.

It appeared that in accordance with Article 138e § 1 of the o.p. (which authorizes to act in a given tax case or another given case falling under the jurisdiction of the tax authorities), if nothing else results from the power of attorney, it is also effective in the proceedings and it is the representative who must be served with the decision on the transformation. Desiring to avoid – as may seem only apparent because of the wording of the indicated provision of Article 138e of the o.p., which is applicable in the course of the audit (Strzelec D., Effectiveness of the power of attorney submitted during tax or customs and fiscal audit in the course of tax proceedings, Tax Review 8/2017)–doubts in that respect, as of 1 January 2019, Article 83(1b) has been added to the u.k.a.s. In accordance with that provision, in the event of establishing a special power of attorney to act with regard to a customs

and fiscal audit, it is deemed that the special power of attorney also includes an authorization to act with regard to tax proceedings (which is a consequence of the previously conducted audit) and in proceedings instigated as a result of an appeal filed, if the auditee has not revoked the special power of attorney.

8 Lack of devolution while hearing the appeal

If the audit is transformed into proceedings, the head of the customs and tax office that has drawn up the results of the audit is competent to conduct the proceedings and issue a decision in that case. During the tax proceedings conducted by those authorities, the provisions of Section IV of the o.p. in connection with Article 94(2) of the u.k.a.s., with the exception of Article 165 of the o.p. regarding the instigation of tax proceedings.

If, following the transformation of a customs and fiscal audit into tax proceedings, a decision regarding compliance with the tax law is issued, an appeal against such a decision shall be examined by the same authorities that issued it, i.e. the head of the customs and tax office (Article 221a of the o.p.). The implementation of such a scheme to hear appeals, which despite the amendment of the provisions has not been modified, raises some vital reservations (Strzelec D., et al: On the Devolution of Tax Proceedings, Tax Review 6/2018, pp. 11–15), which induces to pay attention to two crucial issues.

Namely, on the one hand, as a consequence of introducing such a solution, the decisions of the head of the customs and tax office will be de facto deprived of a control of judicial uniformity by the director of the tax administration chamber and are subject solely to judicial review of administrative courts. Although organizational units have been established in the tax administration chambers to ensure appropriate supervision over quality and uniformity of the tax law application by all subordinate tax authorities, including the head of the customs and tax office; however, the director of the tax administration chamber has limited legal instruments in that respect to influence the uniformity of the decisions rendered by heads of customs and tax offices.

On the other hand, the adoption of that solution may increase the number of litigations in tax matters. Modifications in that respect may not produce the expected effect of shortening tax proceedings either, because the decisions rendered by the directors of tax chambers constituted a certain buffer against ill-considered and incorrectly justified decisions of the heads of tax audit offices. There is justified concern that the role of the currently existing appeal bodies will be taken over by administrative courts. Judicial review of decisions rendered by heads of customs and tax offices and revocation of the decisions however, only in the course of a judicial review, will result, on the one hand, in returning the case to the tax authorities in order to eliminate the evidential or legal errors, on the other hand, however, it may contribute to an additional administrative overloading of courts, thus prolonging the case examination time by administrative courts.

9 Summary

In the scope of a customs and fiscal audit regarding compliance with the tax law provisions, despite cross-reference to the appropriate application of the provisions of o.p., we can distinguish certain differences with regard to a tax audit conducted by heads of tax offices, which constitutes a certain regress with respect to the rights auditees are entitled to. The introduction of a new fiscal administration model, including a new type of a customs and fiscal audit despite subsequent amendments still raises several doubts.

Namely, whether the results of the audit should include a legal assessment of a case being subject to the customs and fiscal audit. The provisions of the u.k.a.s. (Article 82(2)) exhaustively list the elements that the results of the audit should include or refer to the application of the o.p. (Article 290 § 2 point 8 of the o.p. in connection with Article 94(1) of the u.k.a.s.). There is, however, no cross-reference to one of the basic elements of the tax audit report, which is the legal assessment of the subject matter of the audit. In practice, a lack of such an element may significantly prevent the auditee from reaching an informed decision regarding the tax return adjustment.

Another one is related to an attempt to answer the question whether, despite a lack of the obligation to draw up an additional (separate) audit

report from auditing the fiscal books, the audit authorities should not draw up such a report in the course of the audit, using the appropriate reference to Article 193 of the o.p., so as to guarantee the party the right to a fair presentation of the facts and active participation at every stage of the proceedings. Including the findings resulting from the books audit as late as in the results of the audit significantly limits the auditee's chances to present evidence to prove the reliability of the fiscal books.

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PART 3:
INTERNATIONAL FINANCIAL LAW

GENERAL ISSUES

Electronization in Customs Proceedings (In Slovakia)[1]

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Abstract

In paper the authors analyse one of the most significant and fundamental tendencies that has recently been evident in the area of customs, the tendency of electronization of customs proceedings. Based on the exclusive use of digital tools this tendency seeks to make legitimate trading more effective and it also enables for customs administration to ensure that customs rules are observed. As the field of customs administration is broad, this paper analyses the electronic custom proceedings and pays particular attention to evaluation of current state of electronic customs proceedings in Slovakia. The introductory part of the paper focuses on the definitions of legal terms under the recent legal regulation. Analytical part of this paper deals with the issue of electronization of customs proceedings as regulated by the law (EU Custom Code) and applicable in practise.

Keywords: Proceedings; Process; Legal Process; Electronic Customs Proceedings.

JEL Classification: H27; K1; K39.

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1 Introduction

It is natural and understandable that the field of customs administration has been recently facing constant new challenges with regards to trading in the international environment. In this light, every single state endeavored to remove the obstacles which could hinder the growth of international trade. It could be said that customs authorities act as key players in this sphere, since they attempt to maintain the balance between the protection of the state and the support of lawful trade by means of control of movement of goods, effective exchange of information and cooperation at the exterior borders of the European Union. It must be borne in mind, though, that in comparison with the past, when business relations between the states were at a relatively low level and no tax barriers or customs tariffs of any kind existed, in the present era international trade has been increasing rapidly, thereby also affecting the movement of goods. In this respect, customs law should promptly respond to these new challenges and seek to strengthen the competiveness of economic operators, improve the economic environment, and especially, to ensure smooth trade flow and prompt and effective exchange of information (Lyons, 2008: 94; Massimo, 2012: 75).

This challenge and the new direction in the field of customs law was to be supported also by the "electronization of customs communication". It is one of the most significant tendencies that is evident in this field. Such tendency is mainly connected with the development of information and communication technologies. As the customs area is broad, this paper focuses on the issue of electronic customs proceedings with particular accent on challenges and issues arising from the process of modernisation of customs administration.

In paper the authors based on process of analysis, comparison, generalisation and induction of secondary data verify the hypothesis: "electronisation of customs proceedings makes trading more effective" and conclude findings. In final part of this paper the authors also based on existing information sources using abstraction, comparison and synthesis conclude own findings related to existing situation of electronisation of customs in Slovak Republic with particular accent on customs proceedings.

2 Theoretical definition of terms (proceedings, process and practise)

All activities connected with the electronic communication in the field of customs law in Slovakia shall be ensured and coordinated by the Financial Directorate of the Slovak republic. Within the framework of support of the development of electronic communication, the objective of the Financial Directorate of the Slovak republic has been to implement such electronic communication systems that would enable the entrepreneurs to communicate more efficiently, effectively and promptly with the Financial administration of the Slovak republic. This tendency is especially apparent in the area of legal regulation of customs proceedings.

Customs proceedings represents an important social phenomenon. It is a legal phenomenon at the same time, and as such it is subject to constraints of social development. In real practice, electronic customs communication allows to execute the whole customs proceedings by means of electronic communication channels, it means, from reception of customs declaration in electronic format through electronic communication with the financial administration during processing until electronic payment of customs debt.

Electronic customs proceedings aim to significantly reduce the administrative cost of economic operators, shorten the duration of customs proceedings, provide instant and relevant information with regards the international supply chain and enable uninterrupted exchange of information between the countries of import and export.

Before we delve into the electronic customs proceedings as such, it is desirable to delimitate the essence of customs proceedings. Customs proceedings can be seen as a partial issue in the legal regulation of customs law, however, it plays a very significant role in the implementation of substantive customs law. In general, customs legislation is primarily viewed as substantive law, but the procedural aspects of customs law also have an important share. Customs proceedings, their legal aspects, purpose, the overall essence of the proceedings, their commencement, progress and outcome somehow remain outside the focus of the community of legal professionals. The demarcation

of the legal essence of customs proceedings is grounded on the basic definitions and postulates of procedural law. Predominantly, it is necessary to define the terms proceedings, process and legally relevant proceedings. It is important to note here that these terms can be interpreted in different ways. In general, proceedings are taken to denote a certain procedure which requires the participants to take a step-by-step approach to attain the ultimate goal. The legal nature and position of persons in customs proceedings, their aims and objectives in this proceedings, as well as the means that can lead to them, confer certain specific features on this social phenomenon which clearly differentiate it from other types of legal proceedings.

Customs proceedings are legally relevant proceedings, because objective law attributes relevant legal consequences to it (Babčák, 2017: 255). Proceedings are not executed in a haphazard and spontaneous way but based on predetermined rules which are regulated by procedural customs law. In general, procedural law represents a collection of legal rules which regulate social relationships arising in connection with the implementation of rules of substantive law before the public authorities in cases when the decision-making on the content of legal relations, in particular, on the obligations resulting from them, cannot be left at the discretion of natural persons or legal entities. Thus, it creates certain legal forms in which abstract substantive law materializes and transforms into its concrete form.

Legally relevant proceedings stand at the centre of interest of both private and public law. Their nature is determined by the character of social relations realized in the particular branch of law. Some authors deem concrete types of legally relevant proceedings as the integral part of a broader social phenomenon which they label as legal process. This term can be derived from the Latin word *procedere*, which in translation means go before, go forward, advance, result from something. Building on this statement, the conclusion can be drawn that the legal process as such is realized through various types of regally relevant proceedings.

According to V. Babčák (Babčák, 2000: 60; Babčák, 2005: 34), the characteristics of a legal process are as follows:

- it is not realized in a haphazard way but according to predetermined rules stipulated by law,

- it is a specific mode of executing state or public power,
- it must always be examined as an activity which brings a legally relevant outcome,
- the legally relevant outcome is always a certain concrete form of decision,
- within its realization legal relations of procedural nature arise,
- procedural relations are always created in connection with the realization of material legal rules and relations.

When it comes to the definition of the terms process and proceedings and their mutual relationship, it is frequently under consideration especially of theoreticians from the branch of administrative law which is directly connected with the customs proceedings. Theoretical considerations of this issue can be classified into three basic groups in which:

- the terms process and proceedings are considered identical,
- the term process is treated autonomously and at the same time deemed broader in meaning than the term proceedings,
- the term process is treated autonomously and at the same time deemed narrower in meaning than the term proceedings.

The proponents of the first idea build on the simplest approach to this issue. They either completely equate the terms or they do not consider the difference further and without any detailed analysis they use the terms synonymously. This group of authors who unequivocally equate the terms proceedings and process includes J. Girášek (Girášek, 1981: 156) who states that: "In our opinion, the term proceedings in the area of law is identical in content with the term process, the terms differ only in terminology." J. Králik (Králik, 1989: 178) shares a similar view stating that: "*Certain theoretical works of prominent authors place the terms process and proceedings into such positions, where the opinion of the author in relation to these terms is neither explicit nor evident.*"

In connection with administrative proceedings, V. Němec (Nemec, 1975: 288) advocates a different view; he treats the term process broader in its sense and the term proceedings narrower in its sense stating that administrative proceedings denotes "*such procedure (process) which adjudicates on rights, legally recognized interests and obligations of individually determined persons.*" Similar reflections can also be found in the works of K. Tóthová (Tóthová,

1972: 393–394) who claims that "*such proceedings… is administrative proceedings in its own (narrower) sense of the term which the legal literature designates as administrative proceedings.*" The works of M. Máša (Máša, 1980: 112) advocate the view that the terms process and proceedings are not identical and it is necessary to specify their mutual relation. According to him, "*administrative process must be understood as a superior term which comprises more types of administrative procedures*" and "*administrative process is perceived as a term broader in meaning which encompasses more types of administrative procedures.*"

V. Babčák (Babčák, 2005: 35) adheres to the opinion that it is also important to differentiate whether the terms proceedings and process utilize a concrete legal regulation or a branch of law – the scientific discipline. According to him, the term proceedings, to the prejudice of the term process, is more often employed here. The author also points to the fact that concrete legal regulations use the term proceedings in their names or in the text. It concerns, for example, criminal proceedings, administrative proceedings, tax proceedings or customs proceedings.

Regarding the fact that it is a specific area of customs law, we are inclined to accept the view that customs proceedings is a term narrower in meaning than the term customs process (Červená – Prievozníková, 2013). Customs proceedings is only one of the forms of the execution of state administration in the field of customs through customs authorities which, apart from customs proceedings carry out many other activities, for instance, execute and ensure the fulfilment of tasks in the area of combat against illicit import, export and transit of narcotics, psychotropic substances and precursors, protected species of plants and animals; further, in the area of investigation of criminal offences committed in connection with the violation of customs legislation, collection and processing of information for customs statistics and so on. Many legally relevant proceedings (for example, customs control, subsequent control, collection of debts-customs enforcement proceedings or other types of proceedings as a part of customs surveillance over certain goods) are pursued between the relevant customs authorities on one hand, and concrete natural persons or legal entities on the other hand, although, not each type of the processes above can be considered as customs proceedings.

In case the term proceedings is taken to denote a procedure aimed to fulfil the determined aim, in customs proceedings, this aim is to adjudicate on the rights and duties of natural persons and legal entities with regards to import, export and transit of goods (Karfíková – Boháč, 2015; Karfíková, 2018: 47). The aim of customs proceedings is to decide whether and under what conditions the goods which are imported to, exported from and transiting the territory of the Slovak republic, are placed under the proposed customs proceedings or re-export.

3 Electronic customs proceedings

Customs legislation of the EU is embodied in the Union Customs Code (and related acts and supported by the Work Programme in the field of IT)[4] and is directly applicable in the member states which reflects the exclusive competence of the EU in this sphere. Customs authorities enforce equal basic rules and with regards to fulfilment of their tasks to collect revenues and the regulatory protection, all member states are dependent on other member states. This mutual interdependence presupposes close cooperation. At present, customs information systems and the policy of the EU are based on the "decision on electronic customs administration"[5] which was adopted by the Council and the European Parliament in 2008 and on the provisions of the Union Customs Code. The decision on electronic customs administration stipulates the basic principles according to which the member states and the Commission work together on the development, construction and operation of systems supporting customs transactions. These systems concern different customs proceedings including processing of clearances, movement of goods and exchange of information between the administrative authorities. They also include several common databases.

4 Commission Implementing Decision (EU) no. 2016/578 of 11 April 2016, establishing the Work Programme related to the development and deployment of the electronic systems provided for in the Union Customs Code (OJ L 99, 15. 4. 2016, p. 6), which updates the previous version of the Work Programme stipulated in the Commission Implementing Decision (EU) no. 2014/255 of 29 April 2014 (OJ L 134, 7 May 2014, pp. 46–53).

5 Decision of the European Parliament and Council no. 70/2008/EC of 15 January 2008 on a paperless environment for customs and trade (OJ L 23, 26. 1. 2008, p. 21).

The Union Customs Code in the article 6 lays down the creation of Europe-wide electronic customs system – customs environment in a paperless format. "All exchanges of information, such as declarations, applications or decisions between customs authorities and between economic operators and customs authorities, and the storage of such information, as required under the customs legislation, shall be made using electronic data-processing techniques ". Exceptions exist only in cases of so-called "fall-back proceedings" and special types of transports. The aim of these measures is to build extensive communication network between the customs authorities within the EU, between the customs authorities and other public authorities that have competences in the sphere of international trade and between the public authorities and traders. These measures would enable the field of customs administration keep pace with the developing international trade and could significantly contribute to increase of economic competitiveness of the EU. No later than 31 December 2020 individual member states are bound to adopt effective measures to ensure paperless customs and business environment. For several years now, the Slovak republic has secured effective submission of customs declarations in the electronic format within the export procedure and from 1 May 2017 the duty to lodge electronic customs declaration for import concerns every person. This means that any citizen of the Slovak republic who orders goods from a third country in the amount of 22 € for his own needs is obliged to submit documents in electronic format only. Electronic communication with the customs authority requires qualified electronic signature[6] and registration. Alternatively, the shipper is also allowed to arrange it for the buyer.

Electronic customs declaration must naturally satisfy the requirements of technical specification published on the website of customs administration and be accompanied by advance electronic signature. Such electronic communication between the declarant and the customs administration allows to lodge customs declaration, to request the alteration of customs declaration, to request its cancellation; further, to deliver the notice to control goods and documentation, to deliver the decision in customs proceedings,

6 See the Act no. 272/2016 Z. z. on trust services for electronic transactions in the internal market as amended (Act on trust services).

to deliver acknowledgement of exit of goods from the customs territory of the Union, to trace the progress in customs declaration and the option to amend the information in the incomplete customs declaration. Electronic customs proceedings consist of the following stages:

- submission of goods to the customs office and lodging of customs declaration,
- verification of customs declaration (control of documentation and physical control of goods),
- issuance of a decision in customs proceedings.

Electronic customs declaration shall be considered submitted when the message is delivered into the electronic filing system of the Customs Directorate of the Slovak republic.[7] Electronic filing system will automatically generate a notification of filing of an electronic customs declaration. The electronic customs declaration is considered received when it conforms with the technical specifications and contains all required information.[8] Declarant shall receive a notification generated by the information system of customs administration containing reference number of the customs declaration form and transport reference number. It is important to note that decisions in customs proceedings delivered in electronic format, whether about taking or not taking goods into the proposed customs proceedings, are identical with the decisions in paper format. In the event electronic communication in customs proceedings fails to follow the ordinary procedure, the declarant may request information about the progress of customs declaration proceedings from the customs office by electronic means.

The advantages of electronic processing system rest especially in the elimination of the need of paper documentation together with the deterrence to commit fraud which are related to paper processing, the possibility to improve and effectively monitor transit operations, further, to shorten the period of processing of documents at the customs office because customs

7 See the art. 222 Commission Regulation (EEC) No. 2454/93 laying down provisions for the implementation of Council Regulation (EEC) No. 2913 establishing the Community Customs Code.

8 In compliance with the Annex no. 37 of the implementing regulation and Annex no. 2 of the Decree of the Ministry of Finance of the Slovak republic MF SR no. 419/2006 Z. z. which implement certain provisions of the Act no. 199/2004 Z. z. Customs Code as amended.

declaration is lodged in advance in electronic format, etc. Another expected benefit is a more effective control, decrease in the volume of bureaucracy, better use of sources during physical control, more intensive combat against frauds and their detection.

Modernization and electronization of customs proceedings and of the related processes conducted in compliance with the legislation of the European Union can create preconditions to facilitate trade and support digital economy and its improved use within the online provided services of eGovernment (Červená, Románová, 2016: 51) and more comfort for the business.

4 Conclusion

European Union is a large trading block dependent on free movement of goods into and out of the customs union supplemented by free movement of goods in the area of single market (Románová, 2012: 388; Štrkolec, 2015: 42; Lasok, 1998: 110). In 2016 import and export altogether represented approximately 3,5 billion euro which shows how important the business and smooth operation of customs union is for the prosperity of the European Union. In line with it, there were almost 300 million import and export declarations (SDA – single administrative document). Time devoted to customs clearance of goods as well as the speed and reliability of this clearance are the critical factors of productivity and competiveness. Research has proved that shortening the period of transit and clearance at the "customs" by 10 % may increase trade by 2,5 %–5 % which only demonstrates the importance of reasonably proposed and prompt proceedings of customs control. After long-standing joint commitment to strengthen and modernize customs proceedings, the European Union has finally attained a strong position.[9]

The authors conclude that hypothesis as stated in introductory part of this paper is valid as the electronisation of customs proceedings leads to time savings in process of realisation.

9 OECD Trade Policy Papers 21, 42, 118, 144 a 150 a 157 and Djankov, S., Freund, C., Pham, C. S. "Trading on Time", World Bank/Doing Business (2006 a 2008): Report ("Report", 2008, altered in 2010). 6 Hummels, David (2001). Time as a Trade Barrier, Working Paper. Purdue University, USA.

In essence, intensive discussions about the long-term future of the introduction and operation of IT customs systems in the EU have been held since 2016. All previous problems and achievements of the current model of introducing IT have widely been recognized. A clear consensus exists as for the need to continue with the current structures aimed to carry out the ambitious Work Programme of the Union Customs Code in the field of IT which results from the article 6. With regards the up-to-date structures, the existing initiatives for cooperation can be further elaborated and this way assist the concerned member states in developing their vision of digital customs. Certain advancement in determining the possible directions of more efficient and effective development and operation of customs information systems has already been made. However, it seems inevitable to work on a two-directional approach – further pursue the existing approach to cooperation and refine it, as well as to elaborate alternative models of realization in detail. Attention should be paid to the demands of member states with regards to innovative solutions in this field. Both directions should take into account the digital agenda and the general orientation towards common use of services and solutions in the area of IT across various sectors. Considering the complexity and radical nature of IT systems for customs operations within the member states and among them, it appears that every major change would be evolutionary in character and very probably the necessity to take "mixed" solutions instead of one generally valid solution would be desirable. Another very important step in the forthcoming period should be the creation of so-called catalyzation group[10] consisting of concerned member states that would prepare an analysis of yields and costs and evaluate the influence of future measures on the financing of the EU outside the framework allocated for the programme Customs 2020.

10 See the agenda of the Meeting of the Council of the European Union ECOFIN of 7 November 2017 no. 13623/17 and reference to the item "A" no. 13556/17 UD 240 relating to adoption of conclusion of the Council. See the Regulation (EC) of the European Parliament and of the Council No. 1082/2006 of 5 July 2006 on a European grouping of territorial cooperation (EGTC) (OJ L 210, 31. 7. 2006, p. 19).

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The Substitutability of Unfair Contract Terms in Credit Agreements Denominated and Indexed to Foreign Currencies

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Abstract

This contribution deals with the problem of the capacity of the court to replace the unfair term in the loan agreements with a supplementary provision of national law.

The main aim of the contribution is to confirm the thesis, that the court is not entitled to change the condition for which it states that it is unfair despite the conscious and fixed will of the consumer himself. We have used formal – dogmatic approach for this text.

Keywords: Loan Agreement; Loan in Foreign Currency; Banking Law; Consumer Protection.

JEL Classification: K15; K22.

1 Introduction

Loan agreements denominated and indexed to foreign currencies, especially in Swiss franc (CHF), were very popular in the EU New Member States before the crisis. This was due to several reasons – joining the EU appears, by providing direct access to foreign funding, to offer hedging opportunities through greater openness, to lend credibility to exchange rate regimes, and to raise expectations of imminent euro adoption. Also access to foreign currency loans, usually at lower rates than for domestic currency loans, not only affects the choice of currencies but also has influence on the real interest rate as perceived by borrowers (Rosenberg, Tirpák 2008: 7–8, 18). It is stated that foreign currency loan agreements often offered more

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attractive reimbursement characteristic, such as delayed reimbursement schemes. Financial institutions selected a currency that entailed the lowest short-term interest rate (usually Swiss franc). It resulted in the smallest initial instalment for a given amount of loan, what made it accessible to a very wide scope of households, including subprime borrowers (Cyman, 2017: 454–455). As a result of a significant increase in the value of the CHF and the related changes in the amount of credit obligations, the debtors, especially consumers, paying such loans found themselves in serious financial problems.

Some authors point out that doubts concerning the legality of contracts denominated or indexed to foreign currencies appeared only in connection with the change in exchange rates, and the responsibility for these changes should not be charged to banks (Bialek, Niska, 2018: 16–17). However, it should be noted that this problem is quite complex.

Many court cases have become the result of these problems – both on the part of banks claiming against debtors on the one side and on the part of borrowers challenging the reliability of credit agreements, on the other side. As a legal defect in the wording of contracts, debtors indicate, inter alia, a violation of the provisions of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts. The courts in many cases take into account the objections of debtors and recognize the terms of credit agreements as unfair, which leads in accordance with art. 6(1) of the directive 93/13 to the result that these provisions do not bind consumers.

The main aim of this contribution is to confirm the thesis, that the court is not entitled to change the condition for which it states that it is unfair, despite the conscious and fixed will of the consumer himself. Substitution of the unfair contractual term with a court order should take place only in exceptional cases where it is beneficial to the consumer. It is up to the consumers to decide whether this is beneficial for them.

Used scientific methods – formal-dogmatic approach (method). To achieve the aim of the contribution, legal framework and most important judgments of Court of Justice of the European Union and of the various polish courts had been analysed. As a result of the process of performing the analysis, a solution based on this analysis had been developed. A doctrinal

interpretation was made in such a way that the law creates a consistent, axiologically coherent and gap-free system.

Most important books and articles published in previous time: Duivenvoorde, B. The Consumer Benchmarks in the Unfair Commercial Practices Directive, Amsterdam: 2015; Fischer, A. M., Yeşin, P. Foreign currency loan conversions and currency mismatches, SNB Work Matches 4/2019; Rogoziński, D. Orzecznictwo Sądu Najwyższego w sprawie kredytów waloryzowanych kursem waluty obcej a prawidłowa implementacja jurysdykcyjna dyrektywy 93/13/EWG (The Polish Supreme Court's case-law in cases concerning loans indexed with the exchange rate of a foreign currency and the correct judicial implementation of Directive 93/13/EEC), Rozprawy Ubezpieczeniowe. Konsument na rynku usług finansowych nr. 30 (4/2018). Journal of Insurance, Financial Markets & Consumer Protection No. 30 (4/2018).

2 The role and scope of the Directive 93/13 in the system of the consumer protection

The consumers are the important recipients of financial products and services. They are considered unprofessional clients, as they tend to lack sufficient economic, financial and legal knowledge that would ensure equality between the client and the financial institution. Considering above, the European Commission has been undertaking numerous actions aiming to reinforce the legal protection schemes for consumers at the single market for financial services (Szustak, 2014: 115).

The Member States are responsible to ensure that contracts concluded with consumers do not contain unfair terms. The purpose of Directive 93/13/EEC is to approximate the laws, regulations and administrative provisions of the Member States relating to unfair terms in contracts concluded between a seller or supplier and a consumer. The directive is based on the idea that the consumer is in a weaker position than professional seller or supplier – as regards both his bargaining power and his level of knowledge (Cyman, 2017: 458).

In the preamble of the Directive it was pointed out, that generally speaking, consumers do not know the rules of law which, in Member States other than their own, govern contracts for the sale of goods or services. Whereas this lack of awareness may deter them from direct transactions for the purchase of goods or services in another Member State. In the light of those findings, to some extent consumer protection is instrumental to the internal market, in the sense that a high level of consumer protection is meant to increase consumer confidence, leading to more cross-border trade (Duivenvoorde, 2015: 16).

Article 1(1) of Directive 93/13 provides, that the purpose of this Directive is to approximate the laws, regulations and administrative provisions of the Member States relating to unfair terms in contracts concluded between a seller or supplier and a consumer. Under Article 6(1) of the directive Member States shall lay down that unfair terms used in a contract concluded with a consumer by a seller or supplier shall, as provided for under their national law, not be binding on the consumer. The contract shall continue to bind the parties upon those terms if it is capable of continuing in existence without the unfair terms.

However, according to the art. 1(2) of the Direcitive 93/13, the contractual terms which reflect mandatory statutory or regulatory provisions and the provisions or principles of international conventions to which the Member States or the Community are party, shall not be subject to the provisions of the Directive 93/13. According to the thirteenth recital of Directive 93/13, the statutory or regulatory provisions of the Member States which directly or indirectly determine the terms of consumer contracts are presumed not to contain unfair terms. Therefore, it does not appear to be necessary to subject the terms which reflect mandatory statutory or regulatory provisions and the principles or provisions of international conventions to which the Member States are party. In that respect the wording "mandatory statutory or regulatory provisions" in Article 1(2) also covers rules which, according to the law, shall apply between the contracting parties provided that no other arrangements have been established. The Court of Justice held in the judgment *OTP Bank Nyrt.* (CJEU: C51/17, § 70), that 'Article 1(2) of Directive 93/13 must be interpreted as meaning

that the scope of that directive does not cover terms which reflect mandatory provisions of national law, inserted after the conclusion of a loan contract concluded with a consumer and intended to remove a term which is null and void from that contract, by imposing an exchange rate set by the National Bank. However, a term relating to the foreign exchange risk, such as that at issue in the main proceedings, is not excluded from that scope by virtue of that provision. However in paragraph 54 and 66, referring to the judgment *Andriciuc and Others*, C186/16 (§ 31 and the case-law cited), the Court ruled, that a national court must take account of the fact that, having regard to the purpose of that directive, namely the protection of consumers against unfair terms included in contracts concluded with consumers by sellers or suppliers, the exception provided for in art. 1(2) of the directive is to be strictly construed. It follows that the fact that some terms which reflect statutory provisions fall outside the scope of that directive does not mean that the validity of other terms, which are included in the same contract and are not covered by statutory provisions, may not be assessed by the national court in the light of that directive.

3 The CJEU judgments prior to the *Dziubak* case (C-260/18)

In the judgements of the CJEU, it is already well-established that Article 6(1) of Directive 93/13 must be interpreted as precluding legislation of a Member State, which allows a national court, in the case where it finds that an unfair term in a contract concluded between a seller or supplier and a consumer is void, to modify that contract by revising the content of that term (see, inter alia, CJEU: C618/10, § 73; CJEU: C488/11, § 57; CJEU: C482/13, C484/13, C485/13 and C487/13, § 28; CJEU: C26/13, § 77; CJEU: C421/14, § 71). However, The Court of Justice stated, in judgment *Kásler* case (C26/13), that, in certain circumstances, such substitution is consistent with the objective of Article 6(1) of Directive 93/13. That provision is intended to substitute, for the formal balance established by the contract between the rights and obligations of the parties, an effective balance reestablishing equality between them, not to annul all contracts containing unfair terms.

In OTP Bank Nyrt. case (CJEU: C51/17, § 61), the Court stated, referring do the Kásler case (CJEU: C26/13, § 83–84), that if it was not permissible for a national court to replace an unfair term, without which the contract concerned could not continue in existence, with a supplementary provision of national law, the court would be required to annul the contract in its entirety. This might expose the consumer to particularly unfavourable consequences. The consequence of such an annulment is that the outstanding balance of the loan becomes due forthwith, to a degree likely to be in excess of the consumer's financial capacities. As a result, it tends to penalise the consumer rather than the lender who, as a consequence, might not be discouraged from inserting such terms in the contracts it offers. Interpreting the judgment in the case Kásler it should be noted, that given the nature and significance of the public interest constituted by the protection of consumers, who are in a position of weakness vis-à-vis sellers or suppliers, Directive 93/13 requires Member States, to provide for adequate and effective means "*to prevent the continued use of unfair terms in contracts concluded with consumers by sellers or suppliers*" (CJEU: C618/10, § 68; CJEU: C26/13, § 78). The system of protection introduced by the directive is based on the idea that the consumer is in a weak position vis-à-vis the seller or supplier, as regards both his bargaining power and his level of knowledge. Hence the aim of the art. 6(1) is to replace the formal balance which the contract establishes between the rights and obligations of the parties with an effective balance which re-establishes equality between them (see CJEU: C415/11, § 44–45; CJEU: C280/13, § 32–33).

The CJEU accurately noted in the judgment in the case Banco Español de Crédito (CJEU: C618/10, § 69), that if it was open to the national court to revise the content of unfair terms included in such contracts, such a power would be liable to compromise attainment of the long-term objective of Article 7 of Directive 93/13. The Court stated, that it would contribute to eliminating the dissuasive effect for sellers or suppliers of the straightforward non-application with regard to the consumer of those unfair terms, in so far as those sellers or suppliers would still be tempted to use those terms in the knowledge that, even if they were declared invalid, the contract

could nevertheless be adjusted, to the extent necessary, by the national court in such a way as to safeguard the interest of those sellers or suppliers.

This problem was pointed by the CJEU also in the case Kásler (CJEU: C26/13, § 79), but the Court held that it does not follow, that Article 6(1) of Directive 93/13 precludes the national court, in accordance with the principles of the law of contract, from deleting an unfair term and substituting for it a supplementary provision of national law. The Court pointed, that replacing an unfair term with such a provision which, as is clear from the thirteenth recital in the preamble to Directive 93/13, is presumed not to contain unfair terms. In that it leads to the result that the contract may continue in existence in spite of the fact that clause has been deleted and continues to be binding for the parties, is fully justified in the light of the purpose of Directive 93/13 (§ 80–81). It should be recalled that, according to the thirteenth recital in the preamble to Directive 93/13, whereas the statutory or regulatory provisions of the Member States which directly or indirectly determine the terms of consumer contracts are presumed not to contain unfair terms.

In the light of those findings, it might seem, that the national courts are empowered to replace an unfair term only when it is beneficial for the consumer, i.e. when without the replacing this term the contract is invalid. The court would be then required to annul the whole contract. In those circumstances it might expose the consumer to particularly unfavourable consequences. Taking above into account it must be considered that if the annulling of the contract is beneficial for the consumer, court should't replace an unfair term. Furthermore, the consumer, not the court, should decide what is beneficial to him. However, it may cause very serious consequences for the financial sector. In the light of the art. 6(1) of Directive 93/13, however, this is not important for the assessment of unfair contract terms' consequences.

However, it must be considered that, the CJEU in case Pereničová (CJEU: C453/10) stated, that article 6(1) of Directive 93/13 must be interpreted as meaning that the court hearing the case cannot base its decision solely on a possible advantage for one of the parties, in this case the consumer, of the annulment of the contract in question as a whole. The Court

also ruled, that that directive does not, however, preclude a Member State from providing, in compliance with European Union law, that a contract concluded with a consumer by a trader which contains one or more unfair terms is to be void as a whole where that will ensure better protection of the consumer.

In those circumstances replacing the unfair term with a court ruling is still contentious. Empowering a national court in the possibility to replace an unfair term, without which the contract concerned is invalid, with a supplementary provision of national law, should depend on the nature of this supplementary provision. Particularly it is not appropriate to replace unfair terms with provisions arising from acts other than those regulating the issue concerned, only on the basis of analogy (see – controversial judgement of the Supreme Court of Poland – Sąd Najwyższy, of 17 July 2017, SN: II CSK 803/16). It is also not appropriate to modify the contract revising its terms by reference to the general principles of contract law. This would introduce contracts' uncertainty in and would be inconsistent with the aims of the directive 93/13.

It should be recalled that "*as the Court has consistently held, that when national courts apply domestic law, they are bound to interpret it, so far as possible, in the light of the wording and the purpose of directive (…) in order to achieve the result sought by the directive and consequently comply with the third paragraph of Article 288 TFEU. This obligation to interpret national law in conformity with EU law is inherent in the system of the EU Treaty, since it permits national courts, for the matters within their jurisdiction, to ensure the full effectiveness of EU law when they determine the disputes before them*" (CJEU: C377/14).

4 The problem of replacing the unfair term with a court ruling in the judgments of the polish courts

According to Article 3851 § 1–2 of the Polish Civil Code provisions of a contract executed with a consumer which have not been agreed individually are not binding on the consumer if his rights and obligations are set forth in a way that is contrary to good practice, grossly violating his interests (unlawful contractual provisions). This does not apply to provisions setting

forth the main performances of the parties, including price or remuneration, so long as they are worded clearly. If a provision of a contract is not binding on the consumer in accordance with § 1, the parties are bound by the remaining part of the contract.

It should be underlined that the possibility of replacing unfair contract terms by the warding of agreement is indisputable in the polish jurisprudence. The Supreme Court in the resolution of 20 June 2018 (SN: III CZP 29/17), ruled that there is a possibility of removing an unfair contract term, even with ex tunc effect, as a result of a later event, for example the confirmation of unlawful provision by the consumer, or concluding a mutual agreement in which the parties explicitly wish to make a provision effective from the very beginning. It is also possible to change the law in order to affect the contracts already concluded. These acts assume that the provision is ineffective, and therefore have a supplementary character in relation to unfair contract term. Additionally they must each time be assessed in the light of the admissibility with the use of general protective measures. The prevailing view in Polish literature is that instead of the annulled provisions a dispositive ones should be applied (see among others: Łętowska, 2002: 343; Skorupa, 2019: 3. 1. III). Some authors, however, indicate that the substitution of the unfair contract term with a court ruling should take place only in exceptional cases where it is beneficial to the consumer (Trzaskowski, 2017: art. 3851; Kubiak-Cyrul, 2019: art. 3851). By declaring the ineffectiveness of the unfair contract term court can't replace such a term with another provision on the rules of equity (Bednarek, 2013: 773; Ruchała, Sikorski, 2019: Art. 3851, 27).

The problem of the possibility of replacing unfair contract terms by a court ruling was considered by the Polish Supreme Court in its judgment of 14 July 2017 (SN: II CSK 803/16). The court ruled that the establishment of the credit interest in CHF may take place, if there are obstacles with the application of other regulations, on the basis of the provisions of the Art. 41 of the Act of 28 April 1936–Bill of exchange law. On the basis of this provision, it is assumed that the average exchange rate set by the National Bank of Poland is authoritative. The Supreme Court in its judgment of 14 July 2017 (SN: II CSK 803/16), held that it also should

be possible, after declaring the unfair contract's term, to fill the gaps in this contract also a in other situations, namely where the interests of the consumer are threatened and when it is impossible to apply the directly applicable dispositive provision. The Supreme Court pointed also out that the consumer can't be faced with the necessity to choose between two solutions, each of which is ex-definitione unfavorable to him – leaving a disadvantageous gap in the contract on the one hand or accepting another disadvantageous clause on the other one. Taking above into account, the Supreme Court allowed courts to the greater degree than in the Kásler case to replace the provisions of the contracts in which unfair terms were found. At the same time, the Supreme Court, taking into account article 385 § 2 second sentence of the polish Civil Code, declared that the contract' s gap resulting from the unfair term should be filled in to consumer's advantage.

The Supreme Court's point of view expressed in the judgment of 14 July 2017 (SN: II CSK 803/16) raises doubts not only because it allows the court to fill in the contract to a wider extend than this specified in the Kásler case. The dependence of court's intervention into the contract on whether it is beneficial to the consumer, is another problem. Moreover a question arises whether the court is able to assess if it is beneficial for the consumer to perform the contract. On the other hand there are often consumers who want to annul the contract and its performance is contrary to their will.

P. Mikłaszewicz states, that the Supreme Court did not correctly apply the CJEU's case law as it doesn't stipulate the possibility of replacing the unfair contract's terms with the reconstruction of the parties' will resulting from the remaining provisions of the contract (Mikłaszewicz, 2019: art. 3851, 52). D.Rogoziński noted that the Supreme Court suggested to apply, by the way of analogy, legal regulations which usually aren't applied to a loan agreement, as they refer to completely different types of legal transactions. Applying such a far-reaching analogy violates the principle of legal certainty (Rogoziński, 2018: 15).

These doubts seem to be shared by the District Court – Sąd Okręgowy in Warsaw, which in the judgment of 8 August 2018, (SO Warsaw: XXV C 590/16) held, that "*adopting the concept that contract's provisions which are considered as its unfair terms shouldn't be replaced by any other terms is a correct solution*

to the problem confirmed both the in legal regulations" (Civil Code, Art. 3851 § 2, Directive 93/13, Art. 6(1)) and in the case law as well. The District Court – Sąd Okręgowy in Świdnica in the judgment of 13 February 2018 (SO Świdnica: II Ca 583/17), ruled that there is no legal basis for replacing an unfair term with another contractual provision, or for adopting allowed and thus binding a party, amount of money which was previously covered by the unfair term. Furthermore, such an intervention in legal relationship existing between consumer and entrepreneur, which involves replacing unfair contract terms with the fair ones, would undermine the essential function of the Directive, which is consumer protectionAlso the District Court – Sąd Okręgowy in Katowice in the judgment of 7 June 2018 (SO Katowice: IV Ca 54/18), stated that the applying of unfair contract terms results in the invalidity of the contract.

5 Case Dziubak (C-260/18)

District Court in Warsaw, on 16 April 2018 (SO Warsaw: XXV C 1255/17) asked the Court of Justice of the European Union a request for a preliminary ruling, which was registered under the reference number C-260/18, Case *Kamil Dziubak, Justyna Dziubak v Raiffeisen Bank Polska SA*. The court's questions concerned first of all the admissibility of replacing the unfair terms by the court's rulings.

The Advocate General in the opinion presented on 14 May 2019, among others stated that it is for the national court finding the unfairness of the condition of the contract to draw all consequences in accordance with national law in order to ensure that this condition has no effects on the consumer, except where the consumer himself objects to the removal of such condition from the contract (III.A.29). Therefore, the court is not entitled to change the content of the condition for which it stated that it is unfair. Article 6(1) of Directive 93/13 must in fact be interpreted as precluding the regulation of national law, which would allow a national court to supplement that contract by changing the content of that condition (III.A.31). The Advocate General pointed out, that in a situation in which the consumer, faced with the choice between the failure of the entire contract as a result of removing unfair terms and supplementing it with another provision

in order to maintain the contract itself, declares that he prefers to eliminate the entire contract, the second of the conditions required in the Kásler judgment ceases exist. In other words, the court would not be able to recognize that the collapse of the entire contract is particularly detrimental to the consumer, despite the conscious and repeated will of the consumer himself (A.III.67).

The Court of Justice in the judgement of 3 October 2019 (CJEU: C-260/18) held, that 'the system of protection introduced by Directive 93/13 is based on the idea that the consumer is in a weak position vis-à-vis the seller or supplier, as regards both his bargaining power and his level of knowledge. This leads to the consumer agreeing to terms drawn up in advance by the seller or supplier without being able to influence the content of those terms. As regards such a position of weakness, that directive requires Member States to provide for a mechanism ensuring that every contractual term not individually negotiated may be reviewed in order to determine whether it is unfair'.

The CJEU ruled, that "*Article 6(1) of Directive 93/13 must be interpreted as not precluding a national court, after finding that certain terms of a loan agreement indexed to a foreign currency and subject to an interest rate directly linked to the interbank rate of the currency concerned are unfair, from taking the view, in accordance with its domestic law, that that contract cannot continue in existence without those terms because the effect of their removal would be to alter the nature of the main subject matter of the contract*". The Tribunal pointed that the consequences for the consumer of a contract being annulled in its entirety must be assessed in the light of the existing or foreseeable circumstances at the time when the dispute arose, and that, second, for the purposes of that assessment, the wishes expressed by the consumer in that regard are the decisive factor. Thus 'the answer to the first question is that Article 6(1) of Directive 93/13 must be interpreted as precluding gaps in a contract caused by the removal of the unfair terms contained in that contract from being filled solely on the basis of national provisions of a general nature which provide that the effects expressed in a legal transaction are to be supplemented, inter alia, by the effects arising from the principle of equity or from established customs, which are neither supplementary provisions nor provisions applicable where the parties to the

contract so agree'. Hence the CJEU ruled, that "*in the light of the foregoing, the answer to the third question is that Article 6(1) of Directive 93/13 must be interpreted as precluding unfair terms contained in a contract from being upheld where their removal would entail that contract being annulled and the court takes the view that that annulment would give rise to unfavourable effects for the consumer, if the latter has not consented to them being upheld*".

The judgment should be assessed positively. The Court reinforced the pro-consumer interpretation of Directive 93/13 and referred to the doubts arising from misinterpretations of the judgment in the Kásler judgment. The effects of the judgment are far-reaching. The courts' annulment of loan agreements will result in serious problems for banks. Their losses only in Poland can reach billions of euros. The result of the ruling is, inter alia, high fluctuations in the listing of banks on the Warsaw Stock Exchange (Słomski, 2019). Currently in Polish courts, especially in Warsaw, "franc" cases constitute the majority of new court cases in some departments. This causes serious problems in ensuring that courts hear cases promptly.

6 Conclusion

The problem of the permissibility of the court replacing the unfair term with a supplementary provision of national law is important to the system of consumers' protect as well as the financial standing of banks. Most of the court cases are cases in which consumers call for the annulment of contracts, which would result in the statement that they used credit without interest and in many cases already repaid it.

The exclusion of the possibility of replacing unfair contract terms by the courts may result in the annulment of contracts and significant problems for financial institutions granting loans. R.Mroczkowski apty pointed out that "*creating by the banks a financial instrument used for debt financing of transactions on the real estate market, which generates currency risk and encumbering client entirely with that risk, due to its widespread used, has turned against those banks. The foreign currency portfolio of mortgage loans began to threaten not only the solvency of individual banks, but what is worse also the stability of the entire banking sector*" (Mroczkowski, 2017: 488).

The solution to the problem may be the application of Hungarian solutions. It should be noted that the sharp appreciation of the CHF also augmented the number of non-performing loans and increased the credit risk of bank balance sheets. Hence, to undo the burden of further currency shocks, many CEE countries looked to the Hungarian experience of converting Swiss franc mortgage loans to domestic currency loans Croatia, Cyprus, Montenegro, Romania and Serbia followed with similar conversion programs from Swiss franc-denominated loans to other currencies, hereinafter referred to as loan conversion programs. In these programs, households had the choice of converting their Swiss franc mortgage loans to another currency (such as the domestic currency or the euro, i.e., another foreign currency) or maintaining their mortgage loans in Swiss francs (Fischer, Yeşin, 2019: 2).

Another way, besides using Hungarian solutions, is to solve the problem by using arbitration courts and consumer arbitration. It is indicated that a possibility of non-judicial settlement of disputes between the consumer and financial institutions greatly improves the scope and quality of consumer protection (Szustak, 2014: 126; Cyman, 2017 (Wolters Kluwer): 364–365). In Polish court practice, however, there is no apparent will of by both consumers and banks to resolve these disputes through mediation. They prefer to settle the dispute with the banks in court.

The analysis shows that due to the consumer protection system, that the substitution of the unfair contract term with a court order should take place only in exceptional cases where it is beneficial to the consumer. It is up to the consumers to decide whether this is beneficial for them. Adopting the opposite assumption and granting legal protection to financial institutions in a situation where they are responsible for introducing unfair contract terms into contracts, would result in weakening the operation of deficiency sanctions. The CJEU jurisprudence in general confirms this hypothesis, but there are different views in domestic case law, sometimes contradictory to the rulings of the CJEU.

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The Supervision Issues over the Activity in the Entities of the Capital Group. De lege lata and de le ferenda Conclusions[1]

Sebastian Skuza[2], Robert Lizak[3]

Abstract

Despite the process of building social market economy that has been ongoing in Poland since 1989, and the wide range of changes in the area of corporate law, among others adopting the law – Code of Commercial Companies in 2000, the regulations from the area of the so-called holding company law have not been able to be introduced to the national legal order so far. The need to adopt such a solution seems to be indisputable, if even due to the fact that creating a capital group can lead to more efficient activity in all areas, regardless of the ownership structure. While in the management sphere, there are already corporate governance mechanisms in place, which enable adaptation to current needs, in the case of the supervision sphere, the situation is a bit different. The analysis conducted by the Authors leads to an ascertainment that in the pursuant to current corporate law, it is impossible to constantly supervise the activity of companies in a group of companies. The goal of this study is to present results of the analysis of the authors, present a proposal of changes enabling an improvement in exercising constant supervision over the activity of companies in the capital group.

Keywords: Corporations; Corporate Governance; Corporate Law; Capital Group; Supervision.

JEL Classifications: G34; G38; K12; K15; K22; M14; M48.

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1 Introduction

They key component that determines creating a capital group is an intention to improve the efficiency of carried out operations, which in consequence is supposed to lead to an easier achievement of the assumed goal. And it does not really matter, whether this goal is the profit maximization, or protecting the public interest in case of entities oriented on the implementation of the public mission (Act on The Principles of State Property Management: 2016).

Regardless of the ownership structure, as well as the basic functioning goal of individual companies in a capital group, said group can lead to the improvement in efficiency of the operations in almost all fields, including management, organizational, operational, financial and legal one (Nogalski, Waśniewski, Miklaszewska: 2013: 237). Despite the fact that a capital group is a widespread and popular form of conducting business, and the adopted law – Code of Commercial Companies is in force for 19 years, there are still no proper provisions regulating its functioning in the Polish law.

The practice of conducting business often "outruns" legal regulations, and in many capital groups the mechanisms of corporate law enabling adaptation to current needs are already in place, but in the opinion of the Authors, this situation concerns only the management sphere (Skuza, Lizak: 2018: 51–63).

The goal of this study is to assess the applicable law and mechanisms of corporate governance in terms of establishing a possibility to exercise constant supervision over the activity of companies in a group of companies. The consequence of this analysis is presenting *de lege lata* and *de lege ferenda* conclusions.

2 The concept and the essence of concepts of a capital group and supervision in the context of functioning of corporations

In the Polish law, the issue regarding term "capital group" has been phrased in a rather specific way. Despite the fact that the concept of a capital group has a crucial meaning in the area of commercial law, the law – Code of Commercial Companies does not include its definition, does not even use such concept. An analogous situation also appears in relation to the definitions

and concepts, with which a capital group is often identified, i.e. holding company, consortium or a group of companies. In turn, in national law there are at least five legal acts of the statute rank, in which such concept has been used, e.g. the Accounting Act (Article 3 paragraph 1 point 44), the Protection of Competition and Consumers Act (Article 4 point 14), the Corporate Income Tax Act (Article 1a), the Trading in Financial Instruments Act (Article 3 point 18), the Public Procurement Law (Article 24 point 23).

The provisions of law of the group of companies in the area of commercial law are limited to defining, in the law – Code of Commercial Companies, the concept of a parent company (Article 4 § 1 point 4), determining the scope of responsibilities of this company (Article 6), and also the issue regarding contracts concluded between the parent company and a subsidiary company in terms of management of the subsidiary company by the parent company and transferring profits by the subsidiary company (Article 7). To sum up, in the provisions of the law – Code of Commercial Companies, the concept of limited regulation of holding company law has been adopted (cf. justification for the draft law of 28 July 2009 on amending the law – Code of Commercial Companies).

The essence of a capital group seems to be a formal or informal connection between at least two companies in order to maintain control of one company over the second one in all areas of activity, enabling a more efficient and effective implementation of commonly determined economic interest (cf. Gajewski: 2005: 13–17; Kot, Stokłosa: 2015: 16–20; Kondrakiewicz, 2001: 171–177; Piszcz: 2013: 44–55). In the legal doctrine, the definition of a group of companies states that the group is a new economic entity, created by at least two corporations, connected to each other with a relationship of control and subsidiarity – emphasizing the lack of a separate legal personality of the group of companies. The economic goal of the group, as well as its individual companies, is determined by the parent company (Zięba: 2016: 1; Romanowski: 2008: 5).

In the Polish corporate law, a dual model of managing a corporation has been adopted, through the separation between an organizational, personal and functional managerial and supervisory sphere (Kidyba: LEX/el. 2018). The role of the management board is to carry out all affairs of the company

that are not not reserved by law or provision of a contract, or the company statute to the competence of its another body (Article 368 § 1 of the law – Commercial Companies Code). In turn, the role of the supervisory board comes to excising constant supervision over the company's operations in all areas of its activity (Article 382 § 1 of the law – Code of Commercial Companies), and also its representation.

According to the dictionary definition, the concept of "supervision" means controlling or watching over someone or something (Skorupka, Auderska, Łempicka: 1969: 418). In turn, the "control" is checking something, comparing the actual state with the required one (Skorupka, Auderska, Łempicka: 1969: 299). Despite the fact that both concepts are repeatedly used interchangeably, they are not identical with each other. The concept of supervision is a broader concept than control. Because the supervision contains two elements: control as a test of compliance of a given proceeding with a specific pattern and the possibility of interference in the decision-making process (Domański, Jagielska: 2010: 13), and the control can be recognized as a process, which consists of examining an actual state and comparing said state with a pattern or a specific standard of conduct, analysis of possible differences and formulating conclusions (Kałużny: 1997: 17–19).

As it follows from Article 382 § 1 of the law – Code of Commercial Companies, exercising the supervision by the supervisory board should be of constant nature. It means that this supervision should be conducted on an uninterrupted basis and cover not only current, everyday operations, but also the activity in a strategic perspective. *Moreover, constant supervision should* concentrate on assessing the activities already completed, ongoing or only planned. Such approach of the supervisory board can and should include in its scope all spheres of activity of a corporation.

3 Exercising a constant supervision over the activity of the companies in a capital group pursuant to the law – Code of Commercial Companies

In the current legal state, all companies included in a group are separate, autonomous legal entities, "extraneous" to each other. According

to Article 12 of the law – Code of Commercial Companies, at the moment of entry in the register, a corporation gains legal personality and is an autonomous entity operating through its bodies. In the absence of regulations on the issue of a capital group and relations between companies within it, it should be noticed that the above regulation concerns both the parent and the subsidiary company.

In aforementioned statute, there are also no material grounds enabling the supervisory board of a parent company to exercise constant supervision over a subsidiary company, even if both companies conduct joint activities for the benefit of the capital group. It results in that the supervisory board of the parent company can exercise supervision only over the operations of the parent company, and the supervisory board of the subsidiary company only over the operations of the subsidiary company. Therefore, the supervisory board of the parent company cannot interfere at any time and in any activity of the subsidiary company and its supervisory board. The supervisory board of the parent company is also unable to exercise constant supervision over the activity of the companies in a capital group, including:

- reviewing the books and documents of the subsidiary companies;
- requiring for subsidiary companies to provide information;
- receiving explanations from representatives of the subsidiary companies;
- concluding contracts with the supervisory boards of the companies in the group of companies, like in the case of management boards, which makes it impossible to create mechanisms of corporate governance that enable exercising a constant supervision.

4 Exercising supervision over the operations of the companies in a capital group pursuant to regulations other than the law – Code of Commercial Companies

While analysing the issue of exercising supervision in the capital group, the regulations regarding the accountancy and financial reporting cannot be omitted.

Firstly, the provision of the Article 4a of the Accounting Act obliges the heads of the entities and members of the supervisory boards to make it that the financial report, consolidated financial report, report on the activity and report on the activity of a capital group meet requirements provided in this act.

Secondly, Article 55 of the Accounting Act states that the parent entity, having its registered office or place of management on the territory of the Republic of Poland, prepares a yearly financial report of the capital group, which consists of data of the parent entity and entities of all levels subsidiary to it, regardless of their registered office, compiled in such way, as if the capital group constituted one entity. Consolidated financial statement consists of:

- consolidated balance;
- consolidated profit and loss account;
- consolidated cash flow statement;
- consolidated compilation of changes in equity;
- an additional information, including an introduction to the consolidated financial report and additional information and explanations.

Finally thirdly, in Article 63c of the Accounting Act, the legislator defined the requirements that should be met by the consolidated financial report.

Regulations of the Accounting Act indicated above unequivocally show that accounting regulations not only include regulations regarding a capital group, including its definition, but most of all they directly refer to the issues of exercising supervision over the activity in the capital group. There is also no doubt that pursuant to the provisions of the Accounting Act, the supervisory board of a parent company has access to financial data of every company in the group of companies.

Despite the lack of a commonly applicable regulations of holding company law in Poland, there are mechanisms of corporate governance in the managerial sphere present in capital groups, which enable the parent companies to influence the subsidiary companies, access to information, and also implementation of joint operations. These mechanisms are based on the provisions included in the law – Civil Code. Pursuant to the freedom of contract rule, determined in Article 353^1 of the law – Civil Code, each

of the companies included in the group of companies can be a party to the contract with any other company regardless of whether they are in a horizontal or vertical relationship. In practice, these are usually the so-called unnamed contracts (e.g. a holding company contract, service contract, outsourcing contract, agreement, enactment of a capital group), so the ones that are not the named contracts and do not have an autonomous normative basis.

Conclusion of the above-mentioned type of contracts enables using in the managerial sphere of capital groups such mechanisms like e.g. project management, centralization of functions, segment management, and also functioning of the organizational units for corporate governance. Using aforementioned mechanisms in the managerial sphere causes specific effects in the supervisory sphere as well.

Project management is a management model involving effective achievement of the project goals, at the same time reducing risks and ensuring communication between participants of the project. In capital groups, projects are often implemented jointly by several companies, and information on the status of the project implementation on its individual stages is passed to all management boards of the companies participating in the project. Then, each management board presents information on the project to its supervisory board. The director of the project is usually a representative of the parent company. This way, the supervisory boards of all companies within the group have access to the same type of information.

Activities of each company consist of basic business processes (core business), which include e.g. production, distribution or services, as well as support processes, the so-called auxiliary functions, like for example IT, marketing, legal, financial and accounting, administrative, HR and payroll or purchasing functions. The auxiliary processes are rather routine and are practically the same for every company. Centralization of auxiliary functions aims to optimize operating costs of the capital group, acquiring crucial economies of scale and synergy, and also high specialization. Centralization of functions is usually executed in companies, in which the holding company contracts are in force, so contracts that cover all companies in the group of companies. Similarly to the project management, centralization of information

takes place in the parent company, which enables the supervisory board of this company to get acquainted with them and assess this sphere of its activity.

The segment management is one of the management models, and its main rule is the consistent cooperation within the group of companies, which translates to higher integration and coordination of operations of individual business segments. Unlike function centralization that includes support services, the segment management concerns basic business processes. The segment management enables optimization of investment and operational planning, cost savings, unification of strategic decisions and decentralization of operational functions, as well as optimization of human resources across the entire capital group. Usually, the organizational units of the parent company, in which information from the companies of the capital group is collected, are at the head of individual segments in the group of companies. These entities develop a contribution to the report on the activity of the parent company, including information from subsidiary companies, which is presented to the supervisory board of the parent company.

Finally, it is impossible not to mention the organizational units for corporate governance that function in the parent companies. These units exercise supervision, implementing tasks resulting from ownership rights in the companies of a group of companies and in other commercial law companies with the participation of the parent company. The actions of the units for corporate governance consist of executing operations in terms of matters resulting from the provisions of law and rules of the ownership supervision. Main goals of corporate governance include:

- ensuring a transparency of activity of companies with participation of the parent company and their bodies, especially by creating an internal legal governance based on the generally applicable and internal regulations,
- using the corporate rights of the parent company to implement the goals of the economic policy of the group of companies, for example by monitoring companies in the group of companies,
- increasing the operating efficiency, management effectiveness and value of companies in the group of companies.

A specific task of a unit for corporate governance that is worth paying attention to is monitoring companies in a group of companies. Monitoring is the basis for evaluation of activities and correctness of operating of these companies, and enables exercising an efficient supervision. Monitoring the companies in a group of companies also serves to prepare studies of synthetic nature, which cover the assessment of economical and financial situation of the companies in the group.

In practice, a situation can occur quite often, in which the president of the management board of the parent company also acts as a chairman of the supervisory board in one of the subsidiary companies, usually one of the key companies in the group. In this context its worth mentioning that in the current legal state, there are no legal grounds for formal use of data and information acquired during the supervisory board in the activity of the parent company. This means that there is no basis for the president of the board of the parent company, who at the same time is the chairman of the supervisory board of the subsidiary company, to be able to use acquired data and information at the supervisory board of the subsidiary company – in a formal way – in the activity of the parent company.

Referring to the aforementioned provisions of the Accounting Act, it should be stated that the director of the parent company and the chairman of the supervisory board in one person has access to financial data from all companies of the capital group. Furthermore, according to Article 382 § 3 of the law – Code of Commercial Companies, particular duties of the supervisory board include the assessment of financial reports, as well as presenting the yearly written report on the results of this assessment to the general meeting. In practice, it means that the chairman of the supervisory board, who at the same time is the president of the parent company, presents at the general meeting, as the chairman of the supervisory board, the assessment of operations of the company subsidiary to the parent company, in which he is the president of the management board. The president of the management board of the parent company acting as the chairman of the supervisory board of the subsidiary company is no more and no less than the owner and the supervisor at the same time

5 Proposed changes in the field of exercising constant supervision over the activity of companies in the capital group

In the opinion of the Authors, there is an urgent need to immediately introduce the holding company law to the law – Code of Commercial Companies. While it is difficult to find rational arguments against introducing the holding company law, it does not cause any major problems to point out to the arguments that speak for its introduction. Examples of such arguments include, for example:

- more efficient management of the companies in the group of companies, including achievement of statutory goals,
- improvement of the process and accuracy of making decisions based on data and information coming from the companies in the group of companies,
- lowering service costs related to the shaping of corporate governance that enables managing the companies in the group of companies.

In connection with the above, it is proposed to introduce the following amendments to the law – Code of Commercial Companies.

Firstly, in the case of attempting to define a capital group, it is especially worth paying attention to the proposed wording of the normative definition of the group of companies in the draft amendment to the law – Code of Commercial Companies (draft law – Code of Commercial Companies and the law on the National Court Register of 22 March 2010). According to Article 4 § 1 point 5^1 of the project mentioned, a group of companies is "*a parent company and company or companies that are subsidiary to it, remaining in a real or conventional permanent organizational connection, and having common economic interest*".

Secondly, it is justified to introduce an additional duty for the supervisory boards of the parent companies, consisting of exercising constant supervision over the operations of the capital group in all areas of its activity.

Thirdly, it should be possible for the supervisory board of the parent company to exercise aforementioned supervision, including:

- providing members of the supervisory boards of the parent companies with an access to information from the subsidiary companies, including access to their documents,

- allowing members of the supervisory boards of the parent companies to require the subsidiary companies to provide access to data and information, and receiving explanations from their representatives;
- allowing members of the supervisory boards of the parent companies the access to data and information that is the result of work of supervisory boards of the subsidiary companies, including access to their documents, receiving explanations or consulting with them.

Fourthly, it is worth considering to grant members of the supervisory boards of the parent companies an additional, relative to the members of the supervisory boards of the subsidiary companies, remuneration for fulfilling additional duties related to exercising constant supervision over the activity of the companies in the group of companies.

Fifthly, it is proposed for consideration to introduce an obligatory solution for companies listed on the regulated market or even in organized trading, which involves for the person acting as the chairman of the supervisory board in the parent company to be able to focus all of its work only on performing this function. Main reason for adopting such a solution is to enable this person to provide a suitable amount of time for reliable fulfillment of the duties of the chairman of the supervisory board. It would actually be justified for the chairman of the supervisory board of the parent company to fulfil his function in a permanent way that is lasting without interruptions. For example, the chairman of the supervisory board would have a right to participate in the meetings of the management board of the parent company regarding this company and group, developing their strategies or investment plans. Adopting such a solution would enable to gain knowledge about the company and the group of companies, and could have real impact on the efficiency and effectiveness of work of supervisory boards and management boards in the companies and groups of companies. At the same time, the chairman of the supervisory board would have access to data and information in the parent company and other companies in the group of companies. Appropriate remuneration for these people should not be forgotten (C. Jungmann: 2006: 464–466). It should not be surprising that in such situation, the salary of the chairman of the supervisory board of the parent company should be significantly higher than the salaries of other

members of the supervisory board, and even – in the opinion of the Authors – close to the salaries of the members of the management board.

Sixthly, it seems to be justified to introduce legal solutions that enable not appointing the supervisory board in the subsidiary company and entrusting the supervision to the supervisory board of the parent company. For example, it should be noticed that the obligation of creating the supervisory board in a limited liability company applies to only some of the cases. Because in accordance with Article 212 § 1 of the law – Code of Commercial Companies, the right of control serves every shareholder. To this end, the shareholder or shareholder with a person authorized by himself, at any time can review books and documents of the company, prepare a balance for his own use or require explanations from the management board. According to Article 213 § 1 of the law – Code of Commercial Companies, the articles of association of the limited liability company can establish a supervisory board or an audit committee, or both of these bodies. In turn, Article 213 § 1 of the law – Code of Commercial Companies states, that in limited liability companies with the share capital exceeding PLN 500 000 and more than twenty five shareholders, a supervisory board or an audit committee should be established. Taking the above into consideration, it is proposed to adopt amendments to the law – Code of Commercial Companies, worded as follows:

The Code of Commercial Companies of 15 September 2000 (Journal of Laws of 2017, item 1577, as amended) is amended as follows:

- in Article 213a § 4 is added as follows:
  - "*§ 4. For subsidiary companies, the provisions of Article 382 § 1a and 1b shall apply accordingly.*";
- Article 381 is amended as follows:
  - "*Article 381. In the joint-stock company, a supervisory board is established, subject to Article 382 § 1a.*";
- in Article 382 after paragraph 1, paragraphs 1a and 1b are added as follows:
  - "*§ 1a. In the subsidiary company, the supervision over the activity of this company can be exercised by the supervisory board of the parent company, provided that the statute of the subsidiary company constitutes so. The provision of Article 381 is not applicable.*

- *1b. In case when the supervision over the activity of the company is exercised in this company in a way referred to in § 1a, the supervisory board of the parent company is understood as the supervisory board of this company.*".

In opinion of the Authors, it seems justifiable to also add another chapter of *Best Practices of WSE Listed companies*, titled *capital groups*. In this chapter, best practices for companies in a capital group, as well as the group itself would be included. Despite the fact that Best Practices are not a generally applicable law, they perform a crucial role in shaping the corporate governance in Warsaw Stock Exchange listed companies. Changing the Best Practices at Warsaw Stock Exchange is justifiable because making changes to the Code of Commercial Companies may prove to be a difficult task. The fact that it was already attempted, unsuccessfully, to introduce the holding company law to the law – Code of Commercial Companies, speaks for this. In 2009 and 2010, some drafts of amendment of the law – Code of Commercial Companies in this scope emerged (cf. the draft law of 29 July and of 22 March 2010). Changing the Best Practices by introducing a new chapter, titled "Capital group" would establish a position of the capital group and enable starting a discussion again on the need of introducing a holding company law, and with that, influence the acceleration of works on amending the law – Code of Commercial Companies.

6 Conclusion

The review of the provisions of national corporate law results in a conclusion that there are no provisions that enable executing constant supervision over the activity of companies in the group of companies in all fields. The exception is the financial sphere, which is regulated by the provisions of the Accounting Act. Although mechanisms such as function centralization, segment or project management enable concentration of data and information and making decisions based on them in the parent company, and then sharing it with the supervisory board of the parent company, this data and information is indirect and area-selective. In opinion of the Authors, it cannot constitute a sufficient basis to exercise reliable and constant supervision over joint activity of several companies in a group of companies. This situation is undesirable for many reasons. The most crucial of them is that

it makes it difficult for capital groups to efficiently and effectively perform statutory operations.

Occurrence of a double mandate phenomenon in the group of companies involving the same person to simultaneously act as the president of the management board of the parent company and the chairman of the supervisory board in the subsidiary company, also does not allow to exercise constant supervision over the activity in the group of companies. There is simply no legal basis allowing to formally use information and data obtained by the chairman of the supervisory board of the subsidiary company in the activity of the parent company, in which company the same person acts as the president of the management board. This does not apply to the case of presenting to the general meeting the assessment of the activities of the management board of the subsidiary company made by the supervisory board, in which the chairman is the president of the management board of the parent company.

In no way it can be said that the reliable fulfillment of the duty of preparing a yearly, consolidated financial report in the capital group is a constant supervision over joint activities of several companies in a group of companies. It is good that such a solution exists, but it only regulates one of many spheres of activity of companies in a group of companies.

Despite the fact that the supervisory board of the parent company has an extremely important role to play in the group of companies, in the current legal state it is not possible to properly play this role. The supervisory board of the parent company should exercise real supervision over processes implemented both in its own (parent) company, and in the entire capital group, and findings made by the Authors indicate that there is no such possibility at the moment.

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Public Finance and Public Financial Law Institutions in the Context of Digital Economy Development

Imeda Tsindeliani[1]

Abstract

The functioning of the most important institutions of the national financial system of the State is actively introducing such a phenomenon as "fintech" (from the English Financial technology / financial technologies), which, using technologies and innovations, allows modernization of the traditional tools of the financial system of the State and its segments, primarily public finance. Objective is the detection of the list of unresolved issues in the theory of the financial law that exist in relation to the nature of the technologies used and innovation ("fintech") in the field of the public finance and the means of legal regulation of the public finance. We have used these methods: theoretical methods of formal and dialectical logic, empirical methods of the comparison, description and interpretation; legal and dogmatic method of the interpretation. There is no uniform approach to the principles on which the legal regulation of the use of "fintech" in the field of the public finances should be based.

Keywords: Public Finance; Cryptocurrency; Blockchain; Financial System; Financial Right; Financial Law Institutions; Tax System; Budget System; Issue Law; Tax Law; Budget Law; Money; Electronic Cash.

JEL Classification: K39; G20.

1 Introduction

Nowadays, many institutions are more focused on the digitalization. If th e accounts are not true and fair and the assets and liabilites are not fairly presented, it is difficult to assess the management performance, especially

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without using the new technical and technological knowledge. (Mariański, 2018)

The modern State can fully realize practically none of its intended purpose without a stably functioning financial system of the State. The balanced and effectively interacting segments of the public and private finances are theoretically the financial system of the State. In the economic literature, examination of the financial systems of the State is traditionally conducted through two approaches: functional and structural (Ivanova, Pokrovskaya, 2018: 13–15).

It should be noted that in the foreign economic literature different terms are used to refer to two main types of the financial systems (markets): "financial system based on banks" (bank based financial system) and "financial system based on securities market" (market based financial system); "relationship-based financial markets" and "direct access financial markets" (arm's length financial markets), or, briefly, "banking" and "market" (Smyslov, 2006: 13–15).

The examination of the financial system of the State in the framework of the structural approach that prevails in the literature is carried out through an analysis of the aggregate of the institutions and markets that provide services to private and public entities (Horn, 2003: 34). The examination of the financial system of the State is carried out through financial institutions and the markets in which they operate, and the available infrastructure. In turn, within the framework of the functional approach, the financial system is examined through the prism of the following segments: public finance, corporate finance and household finance, the latter itself (corporate and household finance) form the private finance segment.

The characteristic of the modern financial system of Russia and the very nature of modern finance causes undoubted interest.

Describing the modern financial system of Russia, researchers come to the following conclusions:

- the financial system, as a system of the market country, hasn't been completed, since it hasn't completely moved to the market and now it is halfway to a developed modern market. Since the finance are

monopolized, in fact there is a nationalization of the part of the financial system;

- permeation from top to bottom of the ideas of the tax orientation in general, the high centralization of the finance;
- budget money – the most inefficient money in the State;
- the absence of large cash funds in addition to public finance as sources of long-term money (Aganbegyan, 2018; 45).

The above mentioned characteristics of the modern financial system of the State show that its effective functioning as a factor ensuring the stable development of the State has not been fully realized. It should be noted that, up to now, it hasn't been possible to ensure high efficiency of expenditures of the public legal entities and the increase of the target efficiency criteria ensuring the growth of socio-economic development. In the Russian Federation, along with the current system of taxes and fees, a parallel tax system has been formed. It is represented by compulsory payments and is not inferior to the current tax system by its fiscal burden. In fact, there are two parallel systems in the country: a system of taxes and fees, concentrated in the Tax Code of the Russian Federation, and a system of mandatory payments (quasi-taxes), scattered in the separate regulatory legal acts, which in their number exceed the entire set of applicable federal, regional and local taxes and fees. Taxes and fees have received a unified regulatory framework in the legislation on taxes and fees, and the regulatory nature of them is adequately disclosed, but there is no uniform regulatory framework for compulsory payments that are not included in the current system of taxes and fees, but they are not inferior to tax payments (Tsindeliani, 2018: 5–6).

Existing researches into the problems of the public finance efficiency examine it through two factors that determine the functions of the public welfare, namely, vertical and horizontal justice that underlies the State's tax instruments (Atkinson, Stiglitz, 1995: 474–485).

The system of public finances of the State itself is based on three levels: public finances of the federation, public finances of the subjects of the federation and public finances of municipalities. The modern theory of the public finance assumes that public finance has the following basic functions: distributive, redistributive, and stabilization functions (Musgrave

Richard, Musgrave Peggy, 2009: 20–21). The realization of these functions necessitates the use of various tools, including within the budget, fiscal and monetary tools. The effective combination of these tools allows to ensure the maximum satisfaction in the needs of the public goods.

Public and private finance, being interconnected and interdependent segments of the financial system of the State, on the one hand, are economic phenomena, but at the same time it cannot be denied that their functioning and structural features are directly related to the legal and political system of the State. Therefore, it is necessary to say directly that the financial system of the State and its segments are formed and function not only as an economic phenomenon, but also as a legal and political phenomenon.

Modern economic theory defines finance as a system of the monetary relations associated with the formation, distribution and use of the centralized funds of the public legal entities to perform the functions intended for them and decentralized funds of the economic entities and households (Sazhina, 2018: 14). According to Sazhina M. A., the monetary essence of the modern finance is replaced by titles, which are given a virtual character. In other words, finances have become virtual ones. It has become a consequence of the new quality of economic relations is virtualization of the economy, where the product as a basic object of the relations has lost the priority, and financial assets have become the main priority. A vivid example of changes in the nature of the finance is adopted by the Bank of Russia "Main Directions for the Development of Financial Technologies for the period 2018–2020"[2]. In particular, modern trends are associated with the stimulation and development of financial technologies, including:

- low marginality of banking services;
- transformation by the financial market participants their business models and the desire to create ecosystems;
- increase of the financial services penetration due to their digitalization;
- loss by banks of the monopoly on the provision of traditional (payment and other) services, as well as the acquisition by non-financial organizations of a significant role in the financial market;

2 Http://www.cbr.ru/Content/Document/File/35816/ON_FinTex_2017.pdf [cit. 10. 9. 2018].

- banks' desire for partnerships with startups and technology companies. The most perspective financial technologies are considered:
  - Big Data and data analysis;
  - mobile technologies;
  - artificial intelligence;
  - robotization;
  - biometrics;
  - distributed registries;
  - cloud technologies.

The development of the financial technologies modernizes traditional areas:

- *payments and transfers*: online payment services, online transfer services, P2P2 currency exchange, B2B3 payment and transfer services, cloud offices and smart terminals, mass payment services;
- *financing*: P2P consumer loans, P2P business loans, crowdfunding;
- *capital management*: robo-advancing, financial planning programs and applications, social trading, algorithmic trading, target savings services, and others.

It is generally recognized that our society and the very humanity itself is at a new stage of the development, which is regarded as the fourth industrial revolution, the fruits of which we use every day (Klaus Schwab, Nicholas Davis, 2018: 29). In fact, this stage of human development can be called the era of new technologies. Technologies that have already began to influence all spheres of the human life and finances have become an active area of the application of these technologies. As a result, the emergence of new institutions and modernization of the existing ones. The development of new economic institutions, based on new technological breakthroughs of the humanity, undoubtedly affect the existing institutions, which are the subject to change under their influence. Even such a category as money, which is at the heart of finance, has already been losing its material forms of the expression and regulating properties. Alternative tools appear in the economy, which are ready, if not completely, then partially, to be an alternative to this traditional institution. As a result, any alternative to money and the mechanisms of money circulation will affect the basic instrument for regulating economic relations and the financial system of the State as a whole – a monopoly on the issue of currency.

The modern economy is transformed into a digital economy at different rates. In the modern literature various definitions of the category – digital economy – are given. In particular, Lapidius L. V. defines it as a set of the relations developing in the process of production, distribution, exchange and consumption, based on the online technologies and aimed at the meeting the needs of life benefits, involving the formation of new ways and methods of managing and requiring effective tools government regulation (Lapidus, 2018: C.7).

The development of the new technologies and the transition of the mankind to a new stage of the industrial revolution encourages States to conduct a new policy, which is aimed at the transformation of many public institutions and processes. New technologies and the economic relations developing on their basis equally apply not only to private actors, but also directly come into contact with the activities of the State and institutions related to its functioning. In this connection, the Government of the Russian Federation has approved the program for the development of the digital economy of the Russian Federation, in which data in digital form is a key factor of the production in all areas of socio-economic activity, which increases the country's competitiveness, quality of the life of the citizens, ensures economic growth and national sovereignty[3]. Actually, the realization of this program should make the Russian State a competitive participant in the global digital market, since the new industrial revolution and the new technologies introduced by it pose to the State and society, in general, the need to carry out transformations of the entire socio-economic system. As a result, new technological products that are not exhaustive are designated, in particular, by such phenomena as:

- big data;

[3] The decree of the President of the Russian Federation from 9. 5. 2017 N 203 "Strategy of information society development in Russian Federation to 2017–2030" // Sz the Russian Federation. 15. 5. 2017. N 20. article 2901; resolution of the Government of the Russian Federation from 28. 8. 2017 N 1030 "About control system implementation of "Digital economy of the Russian Federation" (together with "Rules of development, monitoring and control of the implementation of action plans for the implementation of the "Digital economy of the Russian Federation") // Sz the Russian Federation. 4. 9. 2017. No. 36. article 5450; Order of the Government of the Russian Federation of 28. 7. 2017 N 1632-p <on approval of the program "Digital economy of the Russian Federation"> // NW. 7. 8. 2017. N 32. article 5138

- neurotechnology and artificial intelligence;
- systems of distributed registry;
- quantum technologies;
- new production technologies;
- industrial internet;
- components of robotics and sensorics;
- wireless technology.
- technologies of virtual and augmented reality, which touch the sphere of public finance.
- quantum technologies;
- new production technologies.

At the same time, the influence of the new technological phenomena can't only partially, but also globally change the traditional elements that form the entire financial system not only of a specific State, but also the global system of the global finance, and not only can, but also are changing it in real time.

The blockchain technology and derivative products associated with its use, such as cryptocurrency has become the most well-known and universally mentioned phenomenon of the new technological products. The blockchain technology itself is a distribution registry consisting of interconnected blocks of a transaction. Transaction blocks are called registry nodes or nodes. In general, they represent a decentralized database designed to store and confirm the reliability of information (Bashkatov, 2017: 24–25). Modern studies on the use of modern technologies in the economy and, in particular, technology in the field of finance, conventionally referred to as "financial technologies", indicate the absence of a legal definition of such a term, but also the absence in national jurisdictions of clearly developed concepts of legal regulation of this sphere. The Russian Federation is only at the beginning of the way to develop a national legal policy to regulate the sphere of "financial technologies". The studies of the development of the network law in the legal system of the State are of great interest for the development of the legal regulation of "financial technologies".

Nevertheless, it is possible to express our views on those segments of public finances, which, undoubtedly, will undergo modernization due to the laws

of the development of the digital economy as an economy, new technologies. It should be recognized that none of the public finance segments will avoid the modernization impact of the digital economy, namely:

- the monetary system of the State and its operation;
- the budget system of public legal entities;
- tax system of public legal entities;
- the banking system of the State, etc.

2 Cryptocurrency

The Financial Stability Board of the Basel Committee on Banking Supervision defines "fintech" as "*technologically supported financial innovations that contribute to the creation of new business models, applications, processes and products that have the potential to have a material impact on the traditional approaches of financial markets and institutions, as well as the procedure for providing financial services*."[4]

The consequences of the introduction of new digital technologies, the emergence and development of new objects based on the public blockchain of such cryptocurrencies like Bitcoin, Lightcoin, Ethereum, etc. (hereinafter referred to as "cryptocurrency") are very relevant, there is a need for legal regulation as tools and relations arising from their use in general. There is a rather lively discussion about the legal nature of cryptocurrency, while one of the most important aspects is the qualification of cryptocurrency as an object of civil rights, which creates conditions for the legal regulation of operations that are subject to cryptocurrency, which will allow for both legal regulation and other no less important relationship issues arising from the use of cryptocurrency. Currently, most countries are trying to deal with the status of cryptocurrency and introduce legal regulation that meets the interests of the State and business.

Cryptocurrency is money. As known, the concept of "money" is an economic substance, thanks to the work of Friedrich A. Hayek, McConnell KR, Brue, S. L., M. Friedman, J. M. Keynes, L. Harris. (von Hayek, 1996: 16) Money

4 See Advisory document of the Basel Committee on banking supervision on the impact of FINTECH developments on banks and Supervisory authorities dated 31. 10. 2017. Available at:: https://www.bis.org/bcbs/publ/d415.pdf

is a special commodity that is the universal equivalent of the value of other goods and services. Modern economics allocates five functions of money:

- Measure cost. Money makes it possible to estimate the value of goods by setting prices.
- Means of circulation. Money plays the role of the intermediary in the exchange process.
- Means of payment. The function of money, allowing the time of payment does not coincide with the time of payment, that is, when goods are sold on credit.
- Means of accumulation and savings. The ability of money to participate in the process of the formation, distribution, redistribution of the national income, formation of the savings of the population.
- The function of world money. It is manifested in the relationship between economic entities: States, legal entities and individuals located in different countries.

It is believed that money performs its task only with the participation of people who use the possibilities of money. It is people who can determine the prices of goods, use money in the processes of realization and payments, and also use them as a means of accumulation. Thus, theoretically, any object that performs these functions can be considered money.

Cryptocurrency is the equivalent of cash. Using the example of the most famous cryptocurrency – Bitcoin – it can be argued that this is an electronic digital equivalent of cash or an institution that will eventually be able to force out cash. If the authenticity of the cash is verified through watermarking, security thread, microchip, with the help of special technical means, etc., in the case of cash, there is no registry that contains transaction records (therefore certain limitations of cash payments, and there is also a centuries-old problem with their counterfeit of both coins and banknotes), in the case of cryptocurrency – bitcoins, the transaction register guarantees their authenticity. In his work, Frederick. A. Hayek "Private Money", even in 1975, proposed a radically new way to achieve monetary stability – a system based on the competition of parallel private currencies. His idea was simple: such currency should be recognized as an ordinary commodity and, accordingly, produced in a market way. In his opinion, "only those currencies

will remain that will best perform the functions of money: serve as a means of payment and save their value over time."

Cryptocurrency does not fall under the concept of the electronic money, because it has a different mechanism of occurrence. Cryptocurrency is issued through the decentralized emission. No intermediates are needed for its transfer from one entity to another (any special subjects banks, clearing centers, etc.). There are no territorial boundaries for transfer. It is possible to convert into fiat currency[5] and there is the impossibility of canceling the transaction. The disclosure of the concept of "cryptocurrency" through the concept of "digital financial asset", I believe, is not entirely successful, since there is some misunderstanding in the difference between such concepts as cryptocurrency and digital assets. Although it is possible, of course, to say that each cryptocurrency is a digital asset in its essence, but they differ in their management method. There are many differences between financial instruments. Digital asset exists in binary format, i.e. binary files are opposed to text files, while text files are a special case of binary files, thus, in the broad sense of the word, any file fits the definition of a binary file. Cryptocurrency is a binding right. According to the legal construction, the rights of obligation are relative legal relations: there are specific participants who are obliged to a certain behavior pursuing a property interest (as opposed to an absolute legal relationship, in which an authorized person is opposed by an unspecified number of persons, for example, in property legal relations, operational management), i.e. in the legal obligations, the obligated person is always opposed to the entitled person.

The relations, which subject is a cryptocurrency, are built by joining the participant to the trading platform on which the cryptocurrency is circulated. In any case, to buy a cryptocurrency, you need to get your own cryptocurrency wallet. A cryptographic cryptocell is a special program that stores keys for transactions performed.

Having analyzed various sources, you can define the concept of a cryptocurrency as follows: it is a digital (virtual) currency, the creation and

5 Fiat money (from lat. Fiat-decree, the indication "so be it")–is the money, the nominal value of which is established and guaranteed by the State, regardless of the value of the material from which the money is made, or in the vault of the Bank (unsecured money).

control of which is based on cryptographic methods (mathematical algorithms), in relation to which full decentralization is established (no external or internal administrator in the network), which guarantees (confirming) the correctness of the system operations, including the inability to influence the transactions of the system participants. The reliability of the transactions is ensured in the network by Blockchain technology (replicated distributed database – distributed registry technology), the algorithms of which allow combining transactions into "blocks" and adding them to the "chain" of existing blocks to ensure that the base of the chain of transaction blocks is invariable using elements of cryptography and successive hashing[6]. Continuity is provided by including in the current block the hash sum of the previous block, which does not allow changing the block without changing the hashes in all subsequent blocks. Mathematical calculations act as a security as a kind of value of the physical world.

Thus, cryptocurrency is a completely new object of the legal regulation, based on fundamentally different approaches that require excellent legal regulation both at the level of the domestic law and at the level of international law. That's why, it will be necessary to define the conceptual apparatus, provide different legal regulation depending on the cryptocurrency function performed (for example, the instability of the cryptocurrency exchange rate carries negative consequences for the purposes of its use in the investment asset (for accumulation purposes) as units of measure and income, as there are certain difficulties for current cryptocurrencies in the form of interest income, since at present cryptocurrency profitability is reduced to speculative income or the cost of a fall; creating conditions for cryptocurrency competition, legal grounds and conditions, and the organization of cryptocurrency mining activities, i.e. creating rules, that protect both private law and public law interests, ensuring national security, in connection with which it is necessary to identify the subjects and provide for responsibility in the event of a possible system failure, authorized or unauthorized changes to the programe code, and also arising in connection with this consequences

6 Hashing is a mathematical transformation of the information. Hashing algorithms are used to verify the integrity and authenticity of the files.

in the system and the procedure for their elimination and restoration of the legal balance.

There is a lot of work to be done in a fairly short time. The world does not stand still and at present there are polar situations where, on the one hand, rapidly developing information technologies are being introduced in all spheres of the life of the society and individual, on the other hand, the lack of timely prepared legal mechanisms, the adoption of which can be late effect, when not the State will control the system, but the system of the State, the creation of a substance competing with public order, through the existence of parallel systems, which can lead to a strong competition and effective development, or vice versa, to stop it. Humanity constantly tried to understand, review the form and role of money. We believe that the task of the current generation is to explain the need and need to transform money into a crypto-virtual form.

Accordingly, this affects the functioning of public finances. As a result, this causes the modernization of the legal regulation of the public finances. A special place in the modernization of the legal regulation belongs to the rules of the public financial law. It seems that in the system of the public financial law, a large group of rules is formed, which form the totality of legal institutions that are transformed into a sub-branch of the public financial law – the issue law.

3 Modern system of the public financial law

The interest in the researching of the financial law system as a branch of the law is due to a variety of the circumstances, primarily the active development of legislation governing public finances, the modernization of the State's economic system in general, and the State's financial system in particular. The available monographs show that this problem was and has been remaining an urgent and called for in the field of the scientific researches (Kazantsev, 2009: 33). The undoubted interest is caused by the approaches of the researchers to the elements that form the system of the branch of the financial law and to the very institutionalization of the branch of law. According to N. Kazantsev, financial law cannot be reduced to a tree

structure, in which many different hierarchical subsystems can be distinguished, having a dendritic (tree) form, which is not a mono-hierarchical, but a multi-hierarchical system, where the highest institution in one hierarchy is lower, on the other – mediating relations with other institutions of the financial law. It is proposed to consider the institute of the financial jurisdiction of the State as such institution.

A. N. Kostyukov notes that the system of the financial law is a body of the parts and elements of the financial law, characterizing its internal structure and isolating it from other branches of the law. The system of the financial law itself is expressed in combining elements of a single legal nature into a structurally-ordered holistic unity, possessing relative independence, stability, autonomy of functioning and interaction with the external environment (Kostyukov, 2002: 27–28). In this case, the mentioned author identifies the grouping of the elements of the financial law system for a number of reasons. In particular, the horizontal structure of the branch of the financial law is characterized by the following elements: financial and legal rules, financial and legal institutions, forming sections and subsectors, which are combined in part of the financial law. Along with the horizontal division of the industry, the said author highlights the vertical construction, which is based on the legal force of financial and legal regulatory material. Based on the analysis, A. Kostyukov represents a system of the inancial law, consisting of two parts: the general and the specific. At the same time, the general part includes the following institutions: rules of the financial law, financial and legal status of the subjects of the financial law, financial relations, legal facts in the financial law, institution of the financial control. The special part is represented by the indicated author consisting of a subbranch of budget and tax law, as well as the following sections:

- State (municipal) revenues;
- State (municipal) expenses;
- banking law;
- insurance activity;
- currency regulation;
- monetary circulation and settlements;
- auditing activities;

- State loan;
- legal regulation of the enterprise finance. In the researches is noted the need to consider the financial law system not only as a horizontal system, but also as a vertical system.

N. M. Kazantsev defines the system of the financial law, consisting of the following sub-sectors:

- mining, production and turnover of the precious metals and stones;
- emissive (bank notes, securities, financial derivatives);
- credit and banking regulation;
- currency regulation;
- accounting;
- tax;
- budget;
- investment;
- insurance;
- financial and estimated;
- regulation of the financial markets;
- collection;
- supervisory and control.

As you can see, the scientists' view of the modern system of the financial law, as a branch of law, does not differ in the uniformity. Scientific ideas about the system of financial law and the elements of its forming are undoubtedly connected closely with the modern legal thinking and well-established conceptual approaches. It can even be said that a schematic approach to the use of the system-structural approach is common.

In the conditions of the development of the digital technologies and the introduction of "fintec" into the sphere of the public finance, it also entails the modernization of the public financial law institutions. The legal means of regulating the most important segments of the public finances are being modernized – the budget system, the tax system, the monetary system, the banking system, and public securities. Accordingly, the structure of the public financial law is being modernized, since the introduction of the new technologies requires a substantial modernization of legal instruments that ensure the regulation of the public finances.

The modern system of the public financial law can be defined through the following elements – the principles of the public financial law, rules of the public financial law, institutions of the public financial law and their associatios. The modern system of the public financial law is represented by such entities as budget law, tax law, emission law, financial control law and public banking law. According to Salachna and Tyniewicki (2017), principle of substantial transparency of public finance (i.e. informing citizens on public funding) has been inadequately implemented and it might be incomprehensible from the social addressee's perspective.

4 Conclusion

Humanity is at a new stage of its development, which is regarded as the fourth industrial revolution. This stage of the human development can be called the era of new technologies, which are already beginning to influence all spheres of human life. Finance has become an active area of the application of these technologies. As a result, the emergence of new institutions and the modernization of the existing ones, based on new technological breakthroughs of the mankind, undoubtedly affect the already existing institutions, which are subject to change under their influence. Money, which is at the heart of the finance, is already losing its material forms of the expression and regulating properties. The alternative tools are emerging in the economy. They are ready to act as alternatives to this traditional institution. The alternative to money and monetary mechanisms will affect the basic instrument for regulating economic relations and the financial system of the State as a whole – a monopoly on the issue of currency. The transition of the humanity to a new stage of the industrial revolution encourages States to implement a new policy that aims to transform many public institutions and processes. At the same time, the impact of new technological phenomena is on the financial system not only of a specific State, but also on the global system of the global finance. As a result, the institutional structure of the public financial law and the legal means of the regulating of the public finances are changing. The modern system of the public financial law can be defined through the following elements – the principles of the public financial law, rules of the public financial law, institutions

of the public financial law and their associations. The modern system of the public financial law is represented by such entities as budget law, tax law, emission law, financial control law and public banking law.

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Preventing the "Artificial Avoidance of Permanent Establishment Status". A Contribution to the Discussion in Results of the BEPS Project

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Abstract

The BEPS project represents the biggest change in international tax law in the 21st century. One of the most important problems addressed as part of BEPS is avoidance of permanent establishment status. The main purpose of this study is to analyze the BEPS project, in particular Action 7 from the perspective of the possibility of counteracting the avoidance of establishment. The thesis will show that despite the successes associated with counteracting tax avoidance under the BEPS project, it has not yet been possible to develop a legal instrument that would prevent the permanent establishment status, in particular as part of the digital economy. The indicated thesis will be demonstrated as a result of the application of methods of analysis of international tax law and the comparative method.

Keywords: Tax; Permanent Establishment; BEPS; Artificial Avoidance of Permanent Establishment Status; International Taxation; Tax Treaties.

JEL Classification: H21; H25; K34; M37.

1 Introduction

Prevention of abuse and circumvention of international tax law is the aim of the *Base Erosion and Profit Shifting*[2] project. It is implementing the initiative to modernize this branch of law. However, the BEPS project itself is not a source of law. It is only a form of international cooperation, agreed by the G20 and OECD countries in order to effectively achieve the assumed

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2 Hereinafter referred to as BEPS.

goal. The concepts of new and updated legal instruments developed under the international BEPS format do not directly bind the participant countries. On the other hand, BEPS results were introduced into the sources of international tax law in an indirect way. First of all, the constructs developed under BEPS have been included in the Multilateral Convention, referred to as MLI[3]. The purpose of the Convention is to replace and supplement selected provisions of bilateral agreements in force heretofore, their counterparts developed under BEPS, without the need to conduct separate negotiations on each agreement[4]. Secondly, regardless of MLI, the results of the BEPS project were implemented into international and national legal systems by modifying the OECD and UN model double taxation conventions[5]. Although the Model Conventions are not a binding guideline for the Member States, they nevertheless form the basis for negotiating bilateral agreements. Thus, the results of the BEPS project directly or indirectly affect the legal orders of almost all countries in the world[6].

The subject of this study is to analyse the results of BEPS, with particular stress on Action 7. It was devoted to counteracting the phenomenon, defined as "artificial avoidance of permanent establishment status". For this reason, the author hereof has undertaken the task of determining to what extent the BEPS project influenced the definition of permanent establishment in the OECD Model Convention as an institution of international tax law. Due to the considerable resemblance to the solutions contained in the OECD Convention, the shape of the definition of permanent

3 The Multilateral Convention (OECD, 2017b) was developed under Action 15 of BEPS as an instrument for the implementation of results of the entire project by modifying relevant norms of applicable bilateral agreements. See, e.g. Valente, 2017: 220; Franczak, 2018: 10.

4 To date, the Multilateral Convention has been signed by 86 countries and territories and is now effective in 15 of them. As regards the other countries and territories, the MLI remains at various stages of the procedure required by the local law for the Convention to enter into force. See http://www.oecd.org/tax/treaties/beps-mli-signatories-and-parties.pdf [cit. 18 1 2019].

5 Formally, this took place in 2017 (OECD, 2017a; UN, 2017).

6 The BEPS time frame is formally outlined in the Action Plan of 2013 and final reports from the fifteen planned actions published in 2015. Currently, a gradual implementation of the legislative measures developed under the project is under way.

establishment in the MLI was also analysed, however to a limited extent[7]. The aim of this work is to prove the thesis that as a result of the BEPS project it was not possible to develop all legal instruments that would comprehensively prevent the emergence of permanent establishment in international tax law. The changes to the definition of a permanent establishment in the OECD Model Convention solve only some of the deficiencies of the institution of a permanent establishment under international tax law. The change in the definition of a permanent establishment in the OECD Convention makes it possible to counteract the artificial avoidance of permanent establishment status. However, the changes developed under BEPS and then implemented into international tax law do not result in the extension of the definition of permanent establishment to activities pursued more and more often via the Internet. Thus, despite the formal termination of the BEPS project, there are still no proposals in international tax law aimed at counteracting all, still occurring, cases of avoiding permanent establishment status in a source country.

The subject of the analysis in this paper are documents developed by the OECD. The basic sources are the OECD Model Convention and MLI and reports on the implementation of BEPS Actions 1 and 7. These documents comprehensively present the problems faced by OECD members in the context of the permanent establishment. Analysis of literature, mainly in English, is of less importance. Therefore, the thesis of the work will be demonstrated using the research method of description, analysis of the most important acts of international tax law, synthesis and comparison with legal regulations in force before 2017.

2 The institution of permanent establishment in tax law

According to the rule expressed in Article 7(1) of the OECD Model Convention, profits of an enterprise earned abroad shall be taxable

7 The provisions of the Multilateral Convention concerning the avoidance of permanent establishment status (Articles 12–15 MLI) are optional. Poland exercised the right to reserve non-application of these regulations and declared that any provisions on the taxation of permanent establishment would be subject to bilateral negotiations. It should be borne in mind, however, that the MLI provisions mentioned above may affect such negotiations, particularly in the case of agreements concluded with countries which have accepted the said provisions.

in the country of its residence (OECD, 2017a: 33). An exception is a situation where an enterprise runs its business through a permanent establishment. In this case, the profits which can be attributed to the permanent establishment may be taxed in the state of its location, i.e. the source country[8]. Such a method of taxation as an exception to the principle of taxation of profits in the country of residence of the enterprise makes permanent establishment one of the most important institutions of international tax law. The setting up of a permanent establishment shall decide on the place of taxation of the part of profits earned by the enterprise (Kobetsky, 2011: 13). However, the legal effects of setting up an permanent establishment go beyond the issue of foreign taxation on the enterprise. They are also important, inter alia, for the place of taxation on such profits as interest, dividends and royalties, and the place of taxation on the remuneration received for employment performed in the source country[9].

Currently, the definition of permanent establishment comprises several independent types of permanent establishment. This is due to the fact that the conditions for the setting up of particular types vary in most cases and do not complement each other[10]. It should be noted that the basic type of permanent establishment, as regulated in Article 5(1) of the OECD Model Convention, is permanent base. Such a facility is a place where the enterprise's activity is wholly or partly carried out outside the place of its residence[11]. On the other hand, a building site, regulated in Article 5(3) of the OECD Convention, is set up as a result of holding a construction site or running construction activity for a period of 12 months outside the place

8 This is so since a country is not required to exercise the right granted in an international agreement.

9 See accordingly: Article 10(4), Article 11(4), Article 12(4) and Article 15(2) of the OECD Model Convention.

10 The literature on the subject distinguish a different number of types of permanent establishment, from two to seven (Skaar, 1991; Mehta, 2012; Schaffner, 2013; Williams, 2014; Lipniewicz, 2017).

11 In Article 5(1) of the OECD Model Convention, the term "business of an enterprise" was used. In the Polish legal language, the term "przedsiębiorstwo" ("undertaking") is understood to mean an organized set of assets (Article 551 of the Polish Civil Code), which by its very nature is not capable of doing business. For this reason, in the Polish article the term "przedsiębiorca" ("enterpreneur", "trader") was used in this work and therefore the entity which may carry out a business and thus have a foreign permanent establishment.

of residence[12]. Another type of permanent establishment is an agency, as provided for in Article 5(5) of the OECD Convention. It uses a dependent agent who works for his principal outside the country of its residence. In the commentary to the OECD Model Convention, service and insurance permanent establishments may be treated as subtypes of an agency permanent establishment under certain circumstances[13]. Regardless of which of the conditions of permanent establishment are met, the legal consequences of its creation will always be identical.

This division is not only of formal character, but entails effects in substantive law. The fulfilment of the conditions laid down in the definition of permanent establishment decides on the place of taxation of profits of the enterprise, including those obtained outside the country of its residence. If a particular factual situation does not fit within the said types, the permanent establishment will not be set up at all. In view of the above, there is a problem of taxation of profits generated outside the country of the enterprise's residence. This will be mentioned later in the study.

3 Artificial avoidance of permanent establishment status according to the BEPS project

The assumptions of the BEPS project have been included in the study *Action Plan on Base Erosion and Profit Shifting,* presented by OECD in 2013 (OECD, 2013). Detailed directions of implementation of the general assumptions have been specified in fifteen areas, referred to as "Actions". The scope of Action 7 included "preventing the artificial avoidance of permanent establishment status". The term "permanent establishment status" used by OECD requires a separate explanation. According to Article 7(1) of the OECD Model Convention, the general rule is the taxation of profits in the country of residence of an enterprise, except in the case where

12 Article 5(3) of the OECD Model Convention. The parties to international agreements often decide to modify the provisions of the convention. For example, double taxation agreements concluded by Poland provide for a period of between 3 and 24 months. See: Kukulski, 2015: 320–324.

13 It should be noted that, unlike the OECD Convention, permanent establishments of service and insurance type were explicitly included in Article 5(3)(b) and of Article 5(6) of the UN Model Convention of 2017.

it operates a permanent establishment in the source country. Importantly, in terms of the subject, both the head office and the foreign permanent establishment constitute the same legal entity. However, as the enterprise has a registered office or seat of the management board in the country of residence, then abroad, that is in the country of the source of its activity, operates in the form of a permanent establishment. This means that an enterprise operating in the area of the source country has a permanent establishment there. Thus, the enterprise has the feature that allows taxation of profits earned in the territory of the source country separately from profits earned in the country of its residence.

Obtaining the "status" at issue depends on whether the conditions included in the definition of permanent establishment are met or not. Definition under Article 5 of the OECD Model Convention determines the form and minimum level of involvement of the enterprise in the source country, which justifies covering it by norms of national tax law of another country than the taxpayer's residence. Obtaining the status of a permanent establishment by a foreign enterprise is therefore dependent on the size and characteristics of its business carried out in the source country.

Limiting or completely avoiding taxation in the source country, i.e. in which the foreign enterprise conducts its business through permanent establishment, may take place by such shaping of this business so as not to set up a permanent establishment. A permanent establishment may be prevented from setting up as a result of one of two actions. First of all, by abusing the norm containing the exclusion of certain forms and types of business carried out in the source country from the definition defining the essential features of the permanent establishment[14]. Second, by circumventing the norm sanctioning the setting up of the permanent establishment in the source country[15]. This norm states that the permanent establishment may only be set up if certain conditions are met. The abuse or circumvention of law takes place, for example, by keeping remote contact with clients by representatives residing in other countries, fragmentation of businesses or operation by formally independent, foreign representatives (Jamroży, 2016a: 65).

14 Referred to as "negative condition".
15 Referred to as "positive condition".

Therefore, as part of the Action Plan of BEPS, a change in the definition of permanent establishment was initiated in such a way as to prevent artificially avoiding permanent establishment status. This took place by the use of exclusions from the definition of permanent establishment and the use of contracts of *commissionaire16*. Thus countries of sources of profits have sought to put a barrier for foreign enterprises taking such actions in their area. To that end, the amendments covered, respectively, Articles 5(4), 5(5) and 5(6) of the OECD Model Convention, which include a definition of agent and a list of exclusions from the definition of permanent establishment. In addition, due to the revision of the above provisions, it was necessary to supplement the elements characterizing permanent establishment in the OECD Convention by paragraphs 4.1 and 8. On the other hand, the new rules include a mechanism to prevent fragmentation, and thus splitting of the business activity, and the definition of a closely related entity, which does not allow considering a business activity fragmented to the extent justified by business reasons as a permanent establishment. The prevention of artificial avoidance of permanent establishment status by dividing business activity also covered issues related to attribution of taxable profit to each type of permanent establishment (OECD, 2013: 32)[17].

Proposals for amendments aimed at preventing the artificial avoidance of setting up permanent establishment in the above-mentioned way are presented in the final report of Action 7 BEPS[18]. The relevant provisions of the OECD Model Convention were subsequently amended. The provisions

16 Contracts of *commissionaire* are similar to Polish contract of "komis" (consignment). They involve the sale of a property by a single entity acting on their behalf, but for a foreign enterprise who owns this property. As a result, only the commission received by the seller is subject to taxation in the source country.

17 It should be noted that the detailed outlining of these problems has enabled Article 5 of the OECD Model Convention to remain unchanged for many years (Skaar, 1991: 560–570).

18 At the turn of 2014 and 2015, extensive public consultation was carried out on the proposed changes to the definition of permanent establishment. More than 100 entities from around the world expressed their opinions on the proposal, including representatives of academia, international consulting corporations, business associations and chambers of commerce (OECD, 2015a). The main part of Action 7 of BEPS on avoiding setting up a permanent establishment was completed in October 2015 (OECD, 2015b). Two and a half years later, OECD presented additional guidance on the rules for assigning profits to permanent establishment, forced by changes to its definition (OECD, 2018a: 8).

amending the definition of permanent establishment in the bilateral agreements already in force have been placed in a separate section of the multilateral convention MLI, entitled "Avoidance of permanent establishment status"[19].

The first element, aimed at preventing the formation of permanent establishment, is to modify the definition of "dependent agent" contained in Article 5(5). According to the OECD Model Convention of 2014, an dependent agent may only be a person who act on behalf of an enterprise, and who holds and habitually exercises an authority to conclude contracts in the source country. Following the changes from 2017, this term has also been extended to individuals who habitually play a central role in the conclusion of agreements which are routinely concluded without significant changes by an enterprise[20].

The change to the OECD Model Convention allowed filling a loophole used for artificial avoiding of permanent establishment status. This avoidance involved unjustified dividing contracting activities into two stages. At the first one, an agent carried out in the source country negotiations about essential elements of the contract. At the second stage, the negotiated draft contract was sent to the headquarters of the enterprise, and thus to the country of its residence, where the contract was formally signed. The contract thus entered into was subsequently performed in the source country (OECD, 2015b: 17). As a result, despite the significant involvement of an agent in the process of contracting, the contract was not finally concluded in the source country, and thus no permanent establishment was set up in that country.

Due to the above-mentioned reasons, the scope of contracts, the conclusion of which results in the formation of a permanent establishment, was also extended. Contracts concluded for the purpose of providing a service by an enterprise and for the transfer of the ownership or for granting

19 See Article 12–15 MLI. The multilateral convention does not correspond to the OECD Model Convention, as it only contains new provisions or those amending existing provisions.

20 The change in the definition of "dependent agent" resulted also in the elimination of the problem of classification of foreign insurance agents who solicit customers and negotiate contracts with them but are not authorized to conclude such a contract. See: OECD, 2015b: 44.

the right to use a property owned by an enterprise, or a property the enterprise has the right to use, have been added to the definition of permanent establishment in Article 5(5) of the OECD Convention[21]. As a consequence, structures using distributors with a limited risk were included in the definition of "agent". These are entities that sell goods on their own behalf, acting at the same time for foreign entities that own the items being sold (Jamroży, 2016b: 105). At the same time, from the term "independent agent" excluded people who act exclusively or almost exclusively for enterprises with which they are closely related. Care was also taken to properly define a closely related person[22]. Therefore, the results of the work undertaken by OECD in the area of preventing *commissionaire* contracts should be assessed positively. The adopted solutions can effectively and comprehensively counteract the phenomenon, known in the case law, of circumventing the definition of dependent agent by using entities that conclude contracts on their own behalf, but for someone else[23].

The second area of OECD's work on avoiding permanent establishment status included a list of exclusions of certain types of activity from its definition. The list of exclusions under Article 5(4) of the OECD Model Convention in its 2014 version contained activities the performance of which did not lead to the formation of a permanent establishment[24]. On the other hand, a separate type of exclusion applied to facilities maintained solely for the purpose of ancillary and preparatory activities. As a result, some enterprises artificially fragmented their coherent businesses so as to take advantage of these exclusions.

The amendments to the OECD Convention developed under the BEPS project assume that the exclusion of permanent establishment status depends

21 Article 12(1) MLI.

22 Article 15(1) MLI. The definition applies to all instruments preventing the artificial avoidance of permanent establishment status, hence also for restricting the exclusions from the definition of permanent establishment and splitting of contracts.

23 For example: Spanish National Court, 9 Feb. 2011, Rec. No. 80/2008 (*Borax*); Spanish Central Economic-Administrative Court, 15 Mar. 2012, Rec. No. 00/2107/2007 (*Dell Spain*).

24 Article 5(4)(a)-(d) of the OECD Model Convention of 2014, including the maintenance of a stock of goods or merchandise belonging to the enterprise solely for the purpose of processing by another enterprise or solely for the purpose of storage, display or delivery.

on whether, as the case may be, the activity run by the enterprise abroad is ancillary or preparatory[25]. In order to prevent circumvention of this rule, a special rule was devised to counter the artificial splitting of activities (Krysiak & Jamroży, 2018: 492). It states that a norm excluding certain activities from a plant definition shall not apply where an enterprise, or entity closely related to it, runs in a given country an economic activity which complements the other and is part of coherent business operations[26].

The solutions presented by the OECD should be assessed positively. They allow an effective reduction in the abuse of exclusions from the definition of permanent establishment and the counteraction of artificial fragmentation of economic activity. These were in particularly frequent in the past, as taxpayers used simplified procedures for the formation of companies and starting up economic activity. The disadvantage of the amendments made to the OECD Model Convention as a result of the BEPS project is to increase the complexity of the definition of permanent establishment. Due to vague phrases such as "habitual contracting", it has also reduced legal certainty. In view of the difference in tax policies of various countries, it is therefore expected that the differentiation in the interpretation of analogous forms of business activity in various countries will increase.

The last element of the work undertaken in the BEPS formula to prevent the artificial avoidance of permanent establishment status relates to building site governed by Article 5(3) of the OECD Convention. Many enterprises practice artificial division of construction contracts in a broad sense (*splitting-up of contracts*). The splitting shall be made between several entities and carried out in such a way that none of them individually pursues their activities for the minimum period required as a criterion for the permanent establishment status. The solution adopted by the OECD assumes that the periods during which closely related entities have carried out their activities at the same construction site or project site are to be aggregated[27].

25 It should also be added that the commentary to the OECD Model Convention was supplemented with the definitions of ancillary and preparatory activities. See: OECD, 2017a: 133.

26 Article 13(4) MLI.

27 Construction works comprise construction and installation activities and supervisory or consultancy activity related to a given site.

This mechanism applies where the activity is carried out within one or more periods which exceed 30 days in total[28]. The concept is relatively simple. It solves the problem, raised in literature for many years, of the economically unjustifiable splitting-up of construction projects between many interrelated subcontractors (Skaar, 1991: 354). It is irrelevant that the clause preventing artificial splitting-up of construction contracts was introduced into the OECD commentary, not directly to the OECD Model Convention (OECD, 2017a: 129–130).

4 Avoiding permament establishment status and business activity run over the Internet

All legal instruments designed to prevent the artificially avoiding of permament establishment status are a response to the problems associated with the current definition of permanent establishment, reported both by OECD member states, judicature and academia (Jimenez, 2016: 467). Assumptions adopted under Action 7 of BEPS have been implemented. Their implementation, however, does not mean a complete solution to the problem of avoiding permanent establishment status. The framework of Action 7 has been strictly and exclusively set up to counteract artificial avoidance of permanent establishment status. Thus, it does not cover all areas of business activity where the phenomenon of avoidance permanent establishment status takes place.

The largest area of business activity that has not been covered by comprehensive regulation in the OECD Model Convention, as regards the status of permanent establishment, is the Internet. The technological development of this medium enables an enterprise to operate in another country without physical presence therein[29]. The literature on the subject mentions a number of features of such dematerialized activity (Jamroży, 2016a: 67–68). Ever

28 Article 14(1) MLI.

29 Business activities carried out using the Internet can be divided into two main areas. The first covers cases of use of the Internet only for making mutual statements but their implementation takes place in a traditional form (e.g. using an website to collect purchase orders for products, which are then physically delivered to the customer). The second area applies to an activity that is carried out wholly on the Internet (e.g. provision of services in the form of advertisement displayed on websites).

increasing scale and forms of Internet use allow today for the formulation of the term "digital economy"[30]. At the same time, the OECD Model Convention there lacks any comprehensive normative regulation relating to permanent establishment status in the case of running a business on-line. This means that there is a structural loophole in the definition of permanent establishment used by OECD. As a result, a permanent establishment is not formed, even despite a considerable level of enterprise's economic involvement in a given country[31]. In this case, avoidance permanent establishment status does not have a nature of artificial action. It has an objective nature and results from the incomplete scope of the definition of permanent establishment. The consequence of this situation is the risk of undermining the effectiveness of the measures to prevent artificial avoidance of permanent establishment status developed under the BEPS formula.

In the absence of a complete normative regulation, the loophole in the definition of permanent establishment should be filled by analogy with existing establishment types. This is the direction of the guidelines contained in the commentary to the OECD Model Convention. They were introduced to the commentary as early as in 2000, so today they can be described as archaic, considering the level of development of current digital economy. Regarding business activities conducted via the Internet, the guidelines from the OECD commentary refer to the construct of permanent establishment of basic type, expressed in Article 5(1) of the OECD Convention. They assume that the main criterion for assessing the emergence of the permanent establishment status is that the enterprise has equipment in the form of a network server. The server must be a fixed facility, located and used to run a business in the source country. The second element necessary to set up an permanent establishment is the connection of the server with the website, i.e. a physical object with an intangible value (OECD, 2017a: 152–153).

30 It should be noted that the OECD's view on the definition of business conducted using the Internet is is not consistent. For example, the title of the BAPS Report 1 contains the term "digital economy" (OECD, 2015 c). The periodic report for 2018 uses the term "digitisation of the economy" (OECD, 2018 a). In fact, digital economy is not a separate branch of economy, but it is merely a term covering the entirety of digitised, on-line activities taken from the real world to the virtual world and activities that exist exclusively on the Internet (e.g. e-sport).

31 E.g. enterprises which run such web portals as eBay, Facebook, AliExpress or Airbnb.

This model of permanent establishment formation doest not fit the modern economy based on transfer of information and the progressive separation of services from the place of their provision. The definition of permanent establishment contained in Article 5 of the OECD Model Convention with respect to Internet activities allows avoidance the formation of permanent establishment. The use of modern technologies such as cloud computing and grid computing leads to a situation where it is impossible to indicate the location of the server. Alternatively, such a location is devoid of any connection with the place where the business is actually run (Lipniewicz, 2015: 194–196). An enterprise often does not own a server, although it actually uses it to run its business outside the country of residence. Thus, the enterprise avoids the formation of permanent establishment, even in the case of major involvement in the economic life of a given country.

The possibility of applying an analogy to the concept of a dependent agent, expressed in Article 5(5) of the OECD Model Convention, to on-line business activity needs to be tackled separately (Lipniewicz, 2015: 198). It provides for the formation of permanent establishment as a result of activities of an agent of a foreign enterprise, but the lack of a server in the source country. Usually, however, Article 5(5) of the OECD Convention will not apply to activities carried out via the Internet (OECD, 2017a: 155). The main reason for this is the lack of an entity that could act as an dependent agent. This is so, because neither the Internet, nor any computer software by which the enterprise operates abroad, is an agent. They are deprived of subjective characteristics. These IT instruments are only a means of intermediation in communicating the will of contracting parties. A provider managing an electronic network in the source country may not be a dependent agent either (Juchniewicz, 2016: 222). Such a provider is responsible solely for ensuring the technical option of concluding contracts remotely. However, it has no right to make declarations of will in order to enter into contracts on behalf of a foreign enterprise. It cannot be also claimed that a provider plays a central role in bringing such agreements into effect. Consequently, it should be stated that the concept of a dependent agent is not an effective tool to prevent the status of permanent establishment being avoided.

The development of information technologies has significantly facilitated the process of minimizing tax burdens. Therefore, the definition of permanent establishment in terms of on-line business does not correspond to current needs. Attempts to fill the gap in the definition of permanent establishment through the use of the construct of a fixed base and of dependent agent cannot bring results. Therefore, the opinion about the crisis of permanent establishment in its contemporary shape seems to be right (Juchniewicz, 2016: 214). The resulting need to prevent the avoidance of formation of permanent establishment has led to covering this legal institution with the amendment implemented in the BEPS formula.

5 BEPS and prevention of the avoidance of permanent establishment status on the Internet

Under the Action 7 BEPS, no specific solutions were proposed relating to the digital economy. The lack of activity in this area stems from the fact that Action 7 deals with the problem of artificial avoidance of a permanent establishment. Running a business via the Internet is not a standalone form of artificial avoidance of permanent establishment. As noted above, the lack of possibility of permanent establishment, despite the enterprise's involvement in the economic life of the source country, results from a structural loophole in the law, not a taxpayer's attempt to circumvent or abuse the law. Filling the gap by analogy can not bring the intended results. In this situation, it is necessary to develop new solutions that relate only to a business run via the Internet. This effort was taken as part of the BEPS.

When analysing the avoidance of permanent establishment status through the use of the Internet, it should be borne in mind that some forms of business activity can be implemented only on-line. These include e.g. selected payment, educational, or medical services. In this case, the general clause against the abuse of international agreements, introduced under Action 6 BEPS (OECD, 2015d), would be excluded. The general clause in question is supposed to prevent abuse of law, not to substitute the contracting states in law making. On the other hand, the remaining BEPS activities in a limited scope refer to the institution of permanent establishment, and as a rule they do not refer to the conditions of its formation.

Action 1 BEPS requires a separate comment. It addresses the challenges related to digital economy (OECD, 2015c). Thus, Action 1 tackles the problem of avoidance of permanent establishment, resulting from the inadequacy of the modern definition to the realities of digital economy. In addition to avoidance of permanent establishment status, Action 1 covered the impact of the Internet on foreign controlled companies and transfer prices. In these cases, the essence of the subject addressed under BEPS was the fact that digital economy goes beyond the legal framework designed for analogue economy. This problem has been well known and has often been addressed in the literature (OECD, 2015c: 106). The literature also proposed various solutions (Jamroży, 2016b: 119–128). They were partly used by OECD, including for the issue of avoidance of permanent establishment status.

The BEPS project identified three potential directions for the development of international tax law as regards mechanisms for the distribution of the right of income taxation in connection with business activities pursued through a permanent establishment (Bask, 2016: 847). The most significant was the profound change in the structure of permanent establishment[32]. It was proposed to use the criterion of "significant digital presence", rather than the physical presence of an enterprise in a source state. A number of criteria would be used to assess the digital presence, including basing the business on services provided on the Internet, on-line contracting, making only electronic payments, absence of physically existing facilities of the enterprise, etc. (Jamroży, 2016b: 125). The departure from the classical concept of permanent establishment for "significant digital presence" would represent considerable progress in preventing the avoidance of establishment status. At the same time, this would not modify the function of permanent establishment under the international income taxation system.

However, a detailed overview of the proposals made under BEPS goes beyond the framework hereof. This effort has already been taken in the literature (Brauner, Baez, 2015; Hongler & Pistone, 2015; Schön, 2018).

32 The second direction involved a wide use of withholding tax on international digital transactions. The third possibility was the adoption of an additional compensatory tax closely related to withholding tax. It would have to be levied on enterprises selling goods and services remotely (OECD, 2015c: 107–117).

However, from the perspective of this study the existing result of Action 1 BEPS should be assessed in the context of avoidance of permanent establishment status. Two key problems concerning international income taxation were identified as part of it. The first one is the rules governing national tax jurisdiction vis-à-vis non-residents. The second problem concerns the principle of attributing profit to a permanent establishment. Due to divergent interests of the contracting States, the first of these problems has not been satisfactorily solved (Jimenez, 2018: 9). However, in the international environment there is consensus as to the need to agree upon a specific solution[33].

The lack of results allowing to comprehensively solve the problem of avoidance of permanent establishment, is caused by a dispute about the distribution of taxation rights between the country of taxpayer's residence and the country of source of its income. In broad terms, it is a conflict between developed and developing countries (Burgers, Mosquera, 2017: 37; Rocha, 2017: 194). Any alteration in the definition of permanent establishment would translate into a change in the proportion of taxation rights. While there is an international consensus on preventing the artificial avoidance of permanent establishment status, there is no consensus as to the revision of the definition and thus preventing of the avoidance of permanent establishment by on-line business activity.

The lack of instant solutions and the depletion of potential tax revenues encourage some States to undertake independent normative action to counteract the avoidance of permanent establishment status. These countries are using the OECD's existing achievements. By way of example, the above-mentioned construct of "significant presence" was used in the official circular published by the Israeli tax authorities in 2016 (OECD, 2018b: 137). It should be assumed that other countries will take similar actions in the coming years, even if they continue to participate in the work forming a continuation of the BEPS project (Becker 2018). This proves serious treatment of the problem of avoidance permanent establishment status by the use of the Internet. However, the results of the previous efforts of OECD in this field

33 It should be noted, however, that the time frame for reaching the compromise was set for year 2020 (OECD, 2018b: 19). Nevertheless, there are doubts expressed in the literature as to the feasibility of a comprehensive resolution of this issue (Lopez, 2015: 13).

are scarce. New constructs have not yet been developed and introduced into the OECD Model Convention.

6 Conclusion

The analysis of actions taken under BEPS in order to prevent the artificial avoidance of permanent establishment status leads to a number of conclusions. They are concentrated around two areas. The first includes measures to prevent artificial avoidance of permanent establishment status, developed under BEPS. The second area concerns the types of activity the performance of which allow an enterprise to continue avoidance permanent establishment status. Regarding the first area, it should be noted that the solutions developed under Action 7 BEPS constitute a qualitative improvement in the definition of permanent establishment. Therefore, the problem of artificial avoidance of permanent establishment status can therefore be considered to be resolved. This concerns preventing the cases of using the institution of dependent agent, exclusions from the definition of permanent establishment and artificial splitting-up of construction contracts. However, this does not mean eliminating all problems related to formation of a permanent establishment. The second of these areas continues to be a challenge, as it includes an inadequate definition of permanent establishment in the context of digital economy.

For all these reasons, the results of the BEPS project related to the prevention of avoidance of permanent establishment status cannot be subject to unambiguous assessment. Admittedly, the OECD states have managed to address the most serious problems associated with misuse and circumvention of the definition of permanent establishment. However, they failed to devise legal instruments allowing for the comprehensive prevention of situations in which no permanent establishment is formed. In this regard, the definition of permanent establishment in the OECD Model Convention is still incomplete after the completion of the BEPS project.

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Ustawa z 29 września 2017 r. o ratyfikacji Konwencji wielostronnej implementującej środki traktatowego prawa podatkowego mające na celu zapobieganie erozji podstawy opodatkowania i przenoszeniu zysku, sporządzonej w Paryżu dnia 24 listopada 2016 r. (Dz. U. z 2017, poz. 2104) (Act of 29 September 2017 on the ratification of the Multilateral Convention implementing measures of treaty tax law aimed at preventing the erosion of the tax base and the transfer of profits, signed in Paris on 24 November 2016); (MLI, 2017).

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FINANCIAL MARKETS

How not to Abuse the Market

Michal Janovec[1]

Abstract

This contribution deals with market abuse as one of the most important regulation of the capital market. Market abuse has been and still is one of the biggest threats of the capital market, because activities like insider trading makes capital market not fair investing area. It's basically information asymmetry all around and moral hazard for insiders, considering using inside information in their own benefit. The main aim of the contribution is to challenge the importance of market abuse regulation and supervision to maintain correct function of the capital market. The question how not to abuse the market could be answered only with good set of regulation and well maintained supervision.

Keywords: Financial Law; Non Fiscal; Capital Market; Market Abuse.

JEL Classification: K20.

1 Introduction

Market abuse has been and still is one of the biggest threats of the capital market, because activities like insider trading makes capital market not fair investing area. It's basically information asymmetry all around and moral hazard for insiders, considering using inside information in their own benefit. The role of capital market regulation and supervision is to reduce such a risks and temptation for those insiders. The future of fair investment environment is the question of good regulation, precious supervision and effective law enforcement in cases of infringement. There are some other threats for the capital market, but I declare market abuse as a biggest of them, not only because its connected with consumer protection but mainly because of its universality for all areas of the capital market. The new and popular

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instruments like virtual currencies or tokens needs market abuse regulation and supervision clear and safe as well. The challenges for the future of the capital market are mostly connected with information asymmetry even more when the role of capital market grows in modern economy and that's why this article analyses market abuse fight as one of the main challenges for the whole capital market.

2 Market Abuse

Generally, market abuse is a forbidden and intolerable activity in the financial market. Such activities are banned as a way of ensuring a level playing field for all economic entities that enter the business. While it is certain that an absolute equality is imaginary, it is desirable to make every effort to get as close to this imaginary ideal as possible.

Market abuse legislation applies in particular to issuers of financial instruments, including new investment instruments regulated under MiFID II, i.e. emission allowances, commodity derivatives, investment instruments traded on over-the-counter markets and the use of benchmarks – reference rates indicators (Husták, 2016).

Market abuse is dealt with in two ways.

- The first way deals with the treatment of inside information about people whom the information concerns (issuers). This way is, as a matter of fact, preventive in its character.
- The second way deals with actual market abuse by someone who has or could have access to inside information.[2]

Today, market abuse is regulated by MAR, which has modified the legal framework in particular by repealing the MAD (Directive 2003/6 /EC). A directive on market abuse (**Directive 2014/57/EU)** was published and approved together with MAR – it harmonises criminal law in connection with market abuse (hereinafter also as the Market Abuse Directive). This legislation

2 According to Art. 7 of Regulation (EU) No 596/2014 (here and after "MAR"): Inside information is information of a precise nature, which has not been made public, relating, directly or indirectly, to one or more issuers or to one or more financial instruments, and which, if it were made public, would be likely to have a significant effect on the prices of those financial instruments or on the price of related derivative financial instruments.

including implementing measures has been in effect since 3 July 2016 (Capital Market Undertakings Act). In the Czech legal regulation, we find the appropriate legal regulation in the Capital Market Undertakings Act, Part IX, Title IV.

There are generally three conditions that constitute market abuse. We can talk about market abuse if someone directly or indirectly inflicts damage on investors. It is someone who:

- used inside information (i.e. information that is not publicly available) – it is a case of insider dealing with insiders being people who have access to inside information;
- manipulated the mechanisms of price setting of financial instruments;
- spread incorrect or misleading information.

Such behaviour can undoubtedly ruin the general level playing field principle for investors. It goes without saying that investors in possession of inside information have a much better starting position than the others, hence the need to use public instruments to redress the imbalance, even though a complete equilibrium remains purely theoretical.

Market abuse can be divided into several areas:

Insider dealing – it is a situation when an insider[3] (a person in the know) has a piece of inside information that is not known to the public (e.g. before a big acquisition is made with which only the company management are familiar, and it is more than likely that such an acquisition will increase the price of the company's shares because it solidifies its financial position; a member of the management then uses the information to their own benefit and buys, for instance, a significant number of shares). This person uses such an information and gains a certain advantage by negotiating a transaction (purchase or sale) with a financial instrument on his/her own account or someone else's. This also applies to the situation where an insider has already issued an instruction for a market transaction and has changed or cancelled the instruction as soon as he has learned the inside information. The special regulation of insider trading deals with the trading of persons

3 According to art. 8 of MAR is an insider person possessing inside information is presumed as a member of the administrative, management or supervisory bodies of the issuer, or has a share of the issuer's capital, or has access to inside information in connection with the performance of a job or in connection with the performance of duties. It could also be a person involved in crime.

with managerial authority (who are also supposed to be consecrated persons), which is discussed below.

Market manipulation – again, it is a situation when an insider spreads untrue or misleading information about, for example, the financial situation of a company while (s)he is in such a position that other people treat the information as completely reliable (it is, for instance, a member of the company's management); the insider can thus influence the share price of the company to their own benefit. These include the closing of transactions and related negotiations, the dissemination of false information through mass media, and the transmission of false or misleading information to benchmarks.[4] The MAR appendix lists indicators that suggest manipulative behaviour associated with false or misleading signals, pricing, use of fictitious means and other forms of misleading or misleading behaviour (Commission Regulation (EU) 2016/522).

Illegal disclosure of inside information – This is a situation, where a person with inside information makes this information available to others if it is not a job or fulfilling the duties. This is regulated by Articles 10 and 14 c) MAR. It can also be a recommendation or guidance by an insider.

In all examples of market abuse people seek their own benefit. They use information that is true but unavailable to others or it is untrue information but from a person who could have access to it.

The fundamental point of the ban on information abuse is at least partial redress of the inequality of access to information; it should help an 'ordinary investor' to improve their position (i.e. their access to relevant information). It is not really possible to forbid employees as well as executives from companies that issue financial instruments to trade in financial instruments; nonetheless, since they could have (and often certainly do have) inside information, their business should be transparent by making it public.

Market abuse refers to an advantage gained because of better access to inside information. EU regulations and legal regulations in member countries attempt to redress this imbalance – there are rules for using, handling and treating inside or misleading information, which constitutes the first legislative way to tackle market abuse, as was stated above.

4 A list of activities that are understood to be market manipulation is given in Article 12 MAR.

As far as the proper treatment of information about issuers of financial instruments is concerned[5], they must, without delay[6], disclose information about themselves.[7]

In addition to such information, the issuer prepares and regularly updates the list of insiders, which it provides to the relevant authority (in our case, the CNB). The reason for this obligation is quite clear and serves in particular to trace and investigate individual violations of MAR, as it contributes to the identification of persons with access to internal information and the time from which they have access to such information. Using this tool, issuers can also generally control the flow of internal information, and thus streamline internal processes such as communication.

Each person on the list confirms in writing his/her familiarity with the duties he / she has through access to inside information, including the acceptance of possible sanctions resulting from violations related to insider trading, or the unauthorized disclosure of inside information (MAR, Art. 18/2).

The European Securities and Market Authority (here and after "ESMA") publishes implementing and recommending technical standards also in relation to the publication of insiders' lists in order to ensure that acts adopted by the European Commission are applied under the same conditions.[8]

Given that only some persons come into contact with inside information, the rationale for the existence of the obligation to publish lists of such persons is quite clear.

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5 A financial instrument is according to Article 124, par. 1 of the Capital Market Undertakings Act defined as an investment instrument admitted to trading on a regulated market of a Member State of the European Union or the admission of which to trading on a regulated market of a Member State of the European Union has been applied for.

6 'Without delay' is according to the accepted interpretation by the courts seen as a sufficient period of time in which the issuer of a financial instrument is able to announce the inside information under the given circumstances and while remaining operational. (See Constitutional Court of the Czech republic: IV. US 314/05 and Supreme Administrative Court of the Czech republic: 3 As 2/2008-152).

7 Publication is mainly on the issuer's website. Then, certainly, the requirement of Article 17(1) MAR will be a rapid approach to correct and timely assessment of information by the public.

8 The format of the Insider List and its update was prepared by ESMA (ESMA 2015: Final Report).

If an issuer shares inside information with a third party while performing the usual business related to the job, this information must be disclosed to the public. The requirement for immediate disclosure of inside information significantly reduces the risk of its abuse; there might, however, be a delay before the information available to someone is announced publicly – that is why there is a legal regulation for insiders regarding inside information.

The regulation says that each person in possession of inside information

- is forbidden on insider trading or attempting to do so is strictly forbidden to share the inside information with someone else unless it is part of the person's practice of profession,
- is forbidden to recommend the acquisition or disposal of financial instruments related to the information,
- is also forbidden to manipulate the market or attempting to do so.

These bans do not apply to trading own shares within buy-back schemes, nor do they apply to measures aimed to stabilise financial instruments.

Every member country is asked to nominate one regulatory and supervisory authority with a common minimum set of obligations. These authorities apply convergent methods to fight market abuse and they should be able to help one another with adoption of preventive measures, especially in cross-border cases. Subsequent administrative co-operation could represent a positive contribution to the fight against terrorism. These authorities are also supposed to co-operate with ESMA (Europa.eu[9]

It is important to mention here also sanctions that can be imposed for market abuse. The European Union attempts to enforce equal sanctions in all its member countries; therefore, in 2014 was adopted a market abuse directive.

By accepting MAR and market abuse directive, the EU laid down a common definition of *actus reus* of crime related to market abuse, e.g. insider dealing, market manipulation and illicit disclosure of information. A new set of criminal sanctions is being created: heavy fines and imprisonment for at least four years are possible sanctions for insider dealing or market manipulation while imprisonment for two years is the punishment for illicit disclosure of confidential information. Furthermore, legal persons are fully liable for

9 Europa.eu. Market abuse [online].

market abuse. Member countries are also required to conduct the judicial proceedings for these crimes if the crime is committed inside their borders or if the offender is their citizen.[10]

3 Director's dealing – dealing of managing persons

The term directors dealing with so-called managerial deals are terms that the current European regulation does not use, but I believe that they still express what the MAR is referring to as a trading of the managing persons, and for this reason I will use these terms for the purposes of this chapter. This adjustment is based on Article 19 of the MAR and was implemented in 2017 do the Czech legal system, as well as in the law of other EU countries.

No one would surely like to trade in securities if the trading could be influenced from the inside. Equal treatment of capital market participants is, therefore, an inevitable condition for its successful operation. The legal regulation of directors dealing notification duty is a specific adjustment in the context of anti-market abuse measures, because in many cases, insider trading is just about the director's dealing. The difference is that insiders are those who have the inside information, whereas the directors/managers are only very likely to receive inside information. Director's dealing without inside information is therefore not insider trading and is subject to certain obligations.

Legal regulation regarding director's dealing primarily attempts to do away with unfair dealing in the capital market. This unfair activity consists in using (or rather misusing) inside information that is not available to all capital market participants. Director's dealing refers to an obligation that applies to people with a specific relation to the issuer of securities, who must notify others of dealings related to the issuer and their securities, including details thereof. Information that people with managing power,[11] as amended are

10 První zprávy. EU stanoví trestní sankce za zneužívání trhu, a může to bolet! [online]. Prvnizpravy.cz [qtd. 22 November 2017] Available at: http://www.prvnizpravy.cz/zpravy/byznys/eu-stanovi-trestni-sankce-za-zneuzivani-trhu-a-muze-to-bolet/

11 In the Czech legislation, the group of persons with managerial authority is mentioned in § 2 par. b) Capital Market Undertakings Act.

required to make public, supplement the notification and information duties that issuers have in general.

Regulation regarding director's dealing is supposed to ensure availability of information about transactions with securities and their derivatives made by people related to a securities issuer. These people have access to inside information about the issuer that is not freely available. While they do not necessarily have to use the information they have got to get some benefit in the securities market, they do have an advantage that can potentially be used in investment dealings.

4 Roots of regulation abroad

The director's dealing regulation comes from the United States (Securities Exchange Act: Sec. 16a). Managers or other employees of the issuer that also possess at least 10 % of the issuer's shares are required to register their name and their position at the issuer with the Securities and Exchange Commission. In case they make any securities transaction, they must report it by the end of the second working day following the day of the transaction. They report the transaction to the Commission and the relevant stock market. The report includes, among other things, the type of transaction, the number of traded securities, the price at which the transaction was realised, and the number of securities that remain in the possession of the person who files the report. Both the report and its subsequent announcement are done electronically. Any profit made from the purchase or the sale of securities – if they have been in possession of the director, the officer or the major stockholder for less than six month – belongs to the company, regardless of the reason behind the transaction. There is one exception, though: if the transaction is made in *bona fide*, i.e. in good faith (Goldstein, 1952).

In the EU law was director's dealing regulated within directive 2003/6/EC (cf. art. 6, par. 4), which has since been replaced by MAR (cf. art. 19) and the market abuse directive. Persons with managerial powers at an issuer and persons closely associated with them are supposed to notify the competent authority of transactions on their own account relating to the securities of that issuer. Individual states must announce this information and make it accessible as quickly and as easily as possible.

5 Obliged Persons

Notification duty applies to the managing persons listed in § 2 par. 1b) of Capital Market Undertakings Act:

- A managing person, defined in § 2 par. 1 a) as a member of the statutory body, statutory body itself, executive director of the company or other person actually directing the activities of the legal entity. When the statutory body or member of statutory body is a legal person, than managing person is the person, representing the legal person at statutory body.
- supervisory body or member of the supervisory body;
- member of the statutory body, statutory body itself, executive director of the company or other person actually directing the activities of the legal entity. When the statutory body or member of statutory body is a legal person, than managing person is the person, representing the legal person at statutory body;
- a person who, within the issuer, makes a decision that may affect the issuer's future development and business strategy and who has the access to inside information.

Before the CNB took over supervision of the capital market[12], this area had been under control of the Czech Securities Commission (hereinafter the CSC), which was heavily involved in these activities at that time. The classification of persons who have the notification duty (according to art. 125, par. 5 of the Capital Market Undertakings Act) was dealt with by the CSC in its statement no. 12/2005. The statement followed Article 6, Section 4 of the 2003/6/EC directive[13], which maintains that the notification duty applies to persons discharging managerial responsibilities within an issuer of financial instruments and persons closely associated with them.

12 The Czech National Bank took over the agenda of the Securities Commission on the 1 April 2006.

13 The Securities Commission followed the European legislation in view of Article 1 of the Capital Market Undertakings Act, which says that law regulates capital markets in harmony with Union norms.

Persons discharging managerial powers are specified in MAR (Art. 3 par. 1, pt. 25):

- a member of the administrative, management or supervisory bodies of the issuer;
- a senior executive who is not a member of the bodies referred to in previous point, who has regular access to inside information relating directly or indirectly to the issuer and power to take managerial decisions affecting the future developments and business prospects of this issuer.

Persons discharging managerial powers have also notification duty for their closely associated persons. According to MAR (Art. 3(1), pt. 26) are persons closely associated with persons discharging managerial powers:

- the spouse of the person discharging managerial responsibilities, or any partner of that person considered by national law as equivalent to the spouse;
- dependent child in accordance with national law;[14]
- other relatives of the person discharging managerial responsibilities, who have shared the same household for at least one year on the date of the transaction concerned;
- a legal person, trust or partnership the managerial responsibilities of which are discharged by a person discharging managerial responsibilities. It could be also the case, when these entities are set up for the benefit of such a person, or whose economic interests are substantially equivalent to those of such persons. The provisions also apply to persons referred to previous points.

6 Which transactions must be made public and how?

Obliged persons according to art. 19 of MAR shall notify to the issuer or the emission allowance market participant, and to the competent authority at the same time, every transaction conducted on their own account relating

14 The term 'dependent children' should be interpreted according to Act on pension insurance, Art. 20/4. The dependent child is defined here until the end of compulsory education and after, not exceeding 26 years of age, if the person is continually preparing for their future profession, or cannot prepare for their future profession or cannot perform employment activities due to a disease or an injury, or due to an unfavourable long-term state of health.

to the issuer's shares or debt instruments or derivatives or other financial instruments linked thereto; It is also an obligation to notify the suspension or lending of investment instruments.

Previous mentioned shall apply to any subsequent transaction once a total amount of EUR 5 000 has been reached within a calendar year.[15] This amount includes all the trades of a person with managerial powers, including trades of closely associated persons. Such notifications shall be made promptly and no later than three business days after the date of the transaction. This obligation is also extended to the suspension or lending of financial instruments by a person with a managerial powers or by a closely associated person.[16]

If an issuer trades on multiple markets, the competent authority is the place of the issuer's registration. The way in which director's dealing is to be reported is again based on the MAR.

The issuer or emission allowance market participant shall ensure that the information that is notified is made public in a manner which enables fast access to this information on a non-discriminatory basis in accordance with the implementing ESMA technical standards. The issuer or emission allowance market participant shall use such media as may reasonably be relied upon for the effective dissemination of information to the public throughout the Union (MAR Art. 19/3). Alternatively, national law may provide that a competent authority may itself make public the information.

Issuers and emission allowance market participants shall notify the person discharging managerial responsibilities of their obligations in writing. Persons discharging managerial responsibilities shall notify the persons closely associated with them of their obligations under this Article in writing and shall keep a copy of this notification.

This provision is a bit skewed in my opinion, but on the other hand, the transfer of the obligation to a particular person is certain administrative relief for both the competent authority and the issuer himself, who already keeps lists of insiders.

15 A competent authority may decide to increase the threshold set out in paragraph 8 to EUR 20 000 and shall inform ESMA of its decision and the justification for its decision, with specific reference to market conditions, to adopt the higher threshold prior to its application.

16 The Trade Notice should contain the elements set out in MAR, Art. 19/6.

Besides above mentioned MAR states, that a person discharging managerial responsibilities within an issuer shall not conduct any transactions during a closed period of 30 calendar days before the announcement of an interim financial report or a year-end report which the issuer is obliged to make public. There is an exception of such a ban on a case-by-case basis due to the existence of exceptional circumstances, such as severe financial difficulty, which require the immediate sale of shares; or due to the characteristics of the trading involved for transactions made under, or related to, an employee share or saving scheme, qualification or entitlement of shares, or transactions where the beneficial interest in the relevant security does not change. Clarification of these exemptions is provided by the European Commission Implementing Regulation.[17]

The duty to notify managerial dealings enables, at least partially, to erase the differences between various levels of inside knowledge about securities issuers. Legislators thus try to create equal opportunities for all capital market participants.

A possible benefit gained unfairly from inside information cannot be eliminated completely, though. Such a situation could occur if there were a ban for certain people on the purchase or sale of an issuer's securities; this would, however, curtail the freedom of enterprise and such people would rightly feel discriminated against.

Another measure adopted in this area is the fact that insider trading has been made punishable by criminal law. This is closely related to managerial dealings. Yet, if obliged persons properly and in due time notify the competent authority of any securities transactions of the issuer, they reduce suspicion of insider trading. The existence of and strict adherence to legal regulations concerning managerial dealings is in everybody's interests, whether it be capital market participants or the obliged persons that are to notify certain securities transactions. Currently, market abuse is regulated by MAR and the market abuse directive. Without any doubt we might say that we can hardly expect anything completely new and ground-breaking by the MAR implementation in the notification duty – rather, the existing regulation

17 Exceptions to this obligation are specified in the European Commission's Implementing Regulation 2016/522.

is going to be extended, specified and updated. What is new and very important, though, is the market abuse directive. It is concerned with the elements constituting market abuse and its criminalisation – the aim is the identical interpretation of what market abuse is, including potential punishment for such activities.

7 Conclusion

I am convinced that new market abuse legislation in Europe definitely fulfils the requirements for the maintenance of fair access to the financial market and its activities there. Among other things, it represents a formal execution of a previously established and promoted strategy to ban strictly any form of market abuse with equal punishment throughout the EU. Such a step appears to be eminently desirable due to frequent cross-border activities of big financial institutions whose impact is truly international. Only by fixing the interpretation of what constitutes market abuse and by agreeing on what punishment can be meted out to the offender in member countries of the EU, can rules regarding the ban on market abuse be internationally standardised, thereby making the international financial market better equipped to provide equal opportunities for investors and consumers. There is no such an important regulation of the capital market like market abuse, because it constitutes equal position for all participants in the area, where so much capital is at stake. Abusing the market is just too tempting in order to earn big money in short term and there is no other threat of the capital market, besides general protection of the capital market existence. The only prevention against market abuse is strong and stable regulation together with strict and effective supervision.

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The Competences of the Polish Financial Supervision Authority in Light of Abusive Clauses in Bank Consumer Contracts

Maciej Mikliński

Abstract

This contribution deals with issues related to the competences of the Polish Financial Supervision Authority with respect to illegal contractual provisions used by banks in consumer contracts. The main aim of the contribution is to confirm or disprove the hypothesis that there are normative solutions enabling the Polish Financial Supervision Authority to appropriately respond to the use of illegal contractual clauses by banks as early as at the stage of introducing them into the legal transactions, without it being necessary to wait for the long-lasting so called abstract control process carried out at the present time by the President of the Office of Competition and Consumer Protection. Scientific methods used, the dogmatic and legal method.

Keywords: Administrative Law; Banking Law; Polish Financial Supervision Authority; Illegal Clauses.

JEL Classification: K23.

1 Introduction

Banks constitute a component of the financial system, participating in the creation of a mechanism for settlements, also accepting and using funds as part of their licensed activity. The non-prescriptive and actual belief is to perceive them as institutions of public trust. This attribute is related to the essence of the operation of banks, namely, organizing financial transactions and guaranteeing the security of the deposited funds (Judgment of the Constitutional Tribunal: P 7/09; Judgment of the Constitutional Tribunal: P 45/12), but also to other features (Pitera, 2007), (Janiak, 2003). The necessity to have sufficient equity, hire experienced managers and supervisory staff, prepare a reliable business plan, and ensure the proper technical

conditions, are some of the many requirements to obtain the required permits sufficient to launch banking operations. In addition, the obligatory supervision over the operations of banks is supposed to ensure the proper operation and stability of this part of the financial market, its transparency, security, protection and trust of the participants. The status of the extensive normative regulation is reinforced by the interpenetration of private and public law norms coupled in all the regulations concerning the financial market (Fedorowicz, 2018: 11). In consequence, from the beginning of their organization, banks are required to strictly comply with the legal norms of both the civil and administrative laws, and in particular, with the restrictions, injunctions and prohibitions arising therefrom, with the awareness of participating in the creation of the financial system and the need to support its stability. Contracts entered into with customers of banks have gained a special meaning in light of the recent financial crisis (Frączek, 2015: 75). It would seem that if banks are entities supervised at every stage of operation, treated in fact as institutions of public trust, they should not engage in any conduct colliding with the good practices and grossly violating the interests of their customers. Such violation would be a manifestation of a disrupted relationship of trust forming the basis of banking operations. Nevertheless, irrespective of the normative objectives and the trust of the supervision authorities expressed, for example, by granting the permit to conduct banking operations, banks repeatedly grossly violate, *inter alia*, consumer rights during the performance of and in connection with their principal licensed activities. They do it only on a widespread basis, from the point of view of the group of individuals affected by such unacceptable practices, not only breaching the good practices of banking imposed by themselves to be followed[1], but most of all, they do it in an exceptionally detrimental manner from the perspective of the fair operation of this part of the financial market, its stability, security and trust of the participants. Such conduct, noticed, publicized and also sanctioned by the President

1 The obligation to respect the ethical values when making economic decisions arises straightforwardly from Clause 1 of the general provisions of the Code of Banking Ethics adopted by the Polish Bank Association. The general rule is complemented a number of detailed provisions, including those requiring fairness and prohibiting banks from using their professionalism in a manner infringing the interests of customers (Clause 1.2, 1.3 of the Code of Banking Ethics.

of the Office of Competition and Consumer Protection is powerful evidence of unacceptable banking practices substantiated by official documents. The scale of breaches and violations is best evidenced by hundreds of illegal contractual clauses, challenged, by nevertheless practised by banks, accounting at some point for 7 % of all the abusive clauses detected (Mikliński, 2016: 80).

The objectives of this contribution include but are not limited to a description of illegal contractual provisions used by banks in Poland as an issue threatening to destabilize this part of the financial market and determining the extent of the powers of the Polish Financial Supervision Authority to appropriately respond to the application of illegal contractual provisions by banks at the stage of their introduction into legal transactions. The assumed research hypothesis was that the Polish Financial Supervision Authority had the legal measures and the competences to protect the participants of the financial market against the use of illegal clauses without the need to wait for the outcome of the long-lasting process, if any, of the abstract control of the general terms and conditions of contracts, contract templates, regulations contrived by banks for transactions with customers. The dogmatic and legal method was employed when preparing this contribution.

2 Illegal contractual provisions used by banks

Banks, as entities entering into contracts on a widespread basis, use contract templates, terms of contracts and regulations in their activity. This is required by the rapidness of transactions, including the requirements for legal transactions that are recurrent in terms of essential issues. Contracts in transactions with consumers including, but not limited to, credit facility and loan agreements, are basically executed using prepared contract templates. It is also stipulations defining the rights and obligations of the parties arising out of the general terms and conditions of contracts and from the regulations to which the contract templates refer. They have the nature of non-prescriptive factors defining the contractual obligations, additional with respect to the principles of social coexistence and established customs (Bednarek, 2013). This practice which has been seen since

the 19th century, leading to the formation of the so-called adhesive agreements, entails the temptation for the stronger party to the legal relationship to impose such solutions in contract templates, contract terms and conditions or in regulations that are characterized by a flagrant and unjustified advantage for the party that is unilaterally formulating them. As a result, the deficiencies in the so-called trade fairness with respect to consumers have met with the legislative authority's reaction, eliminating or mitigating, by way of normative solutions, the effects of using provisions that have not been negotiated individually and which evidently violate the interests of the weaker party to the legal relationship. The problem was discussed to be resolved in different legal bases in EU (Hasselink, Loos, 2012) and could be spotted in different countries like Iceland (Méndez-Pinedo, 2014) or Romania (Pirvu, Duminicâ, Nenu, 2014). At the present time, with certain exceptions of an intertemporary nature, it is the President of the Office of Competition and Consumer Protection who decides that a specific provision should be considered as an illegal contractual provision, and it was the District Court in Warsaw, the Court of Competition and Consumer Protection that would resolve such issues by 17 April 2016. The implemented change, transferring the competences in the discussed scope between the judicial and administrative authorities, notwithstanding all the doubts raised thereby (Nadolska, 2017: 112) is consistent with Article 2 of Directive 2009/22/EC of the European Parliament and of the Council on injunctions for the protection of consumers' interests (Codified version) and Article 2 of the preceding Directive 98/27/EC of the European Parliament and of the Council on injunctions for the protection of consumers' interests allowing the competence of courts or administrative authorities in this respect. Certain generalisations can be made from the analysis of the rulings delivered by the court the other day, and the decisions of the President of the Office of Competition and Consumer Protection delivered at the present time with respect to banks. To be considered illegal, each such clause must fulfil the statutory requirements stipulated in Article 3851(1) of the Civil Code, i.e. this provision shall be addressed to consumers, it shall not relate to the principal (clearly formulated) performance, it shall not be an individually agreed provision, and it shall define the rights and

obligations in a manner contrary to the good practices, grossly violating the consumer's interests. The gravity of breaches made by banks imposing illegal contract clauses upon consumers seems to be different from the point of view of the impact on the bank's stability, and in a certain perspective, also on the security of this part of the financial market. An attempt can be made to categorize these breaches from the point of view of the degree of negative effects that may be associated with their occurrence. The abusive clauses include also clauses the significance of which is minor in this respect. For example, clauses imposing upon consumers, in an unacceptable way, the jurisdiction in case of a dispute[2], stipulating that complaints may be filed within 14 days only from the date of the cause, or refusing to open a savings account without giving a reason[3]. Violations in this respect may render negative consequences, including the need to pay certain costs, penalties, nonetheless, considering the rules of imposing fines and penalties, they will not be significant enough to disturb the stability of a bank. The illegal contract provisions also include such clauses which, when contested, and consequently deemed as non-binding in a specific legal relationship, may arouse more concerns regarding the stability of the bank that used them. Examples include clauses: allowing banks to withhold overpayments of consumers[4], excluding or limiting the liability of banks for damages that may have been incurred by the consumer in his or her relations with the bank, making a declaration of will with the effect as of the moment of sending, notifying or upon expiry of the time from the date of sending the correspondence[5], reserving banks the right to refuse to provide services without giving a reason[6], preventing consumers from withdrawing a placed order[7] or restricting

2 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 1357, 1853, 2190, 3020.
3 The clause entered in the Register of Prohibited Clauses under the number: 2850.
4 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 157, 1804.
5 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 1826, 1861, 2141, 2363, 3174, 4312.
6 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 2594, 4786.
7 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 2224,2235, 2552, 3950.

consumers access to their accounts[8]. They undermine the essence of trust in the bank, and thus, they act destructively on the foundation of this part of the financial market, which may also result in a number of troublesome consequences for a particular bank, for example, related to the effects of the bank failing to effectively make a declaration of will. Nevertheless, assessing them in a reasonable manner, it cannot be considered that they could disturb the proper functioning of this part of the financial market, if they occur sporadically in small banks. Nonetheless, it is also possible to notice a category of illegal contract provisions which, when contested, may have very severe consequences for the position of not only a specific bank, but also this part of the financial market. The negative effects are difficult to estimate. An example are abusive clauses ordering repayment of loan instalments indexed by a foreign currency exchange rate according to the currency sales rate in a given bank[9], general reservations about the possibility of changing the loan interest rate[10], or requesting a change or termination of the contract for generally stated reasons[11]. The existence of illegal clauses in consumer banking contracts is not only an example how banks abuse their position, but above all, it is a severe risk factor for this part of the financial market.

3 Risks related to illegal contract clauses applied by banks in consumer contracts

Risks associated with the inclusion of abusive clauses in bank contracts materialize in several spheres. Most of all, they affect the scope of the civil law relationship between the bank and the consumer. The certainty provided by a joint declaration of the parties' will as to becoming bound by a legal bond including specific rights and obligations indicated in the wording of a legal transaction, the provisions of the law and the regulations forming

8 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 1744,1866,1880, 2277, 3510.

9 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 5743, 3178, 3179, and also the decision of the OCCP President no. DOZIK-9/2018 z 31. 12. 2018.

10 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 2060, 4107, 4704 5622.

11 For example, clauses entered in the Register of Prohibited Clauses under the numbers: 268, 1928, 2151, 2152, 2268, 3180, 5508.

the legal relationship is destabilized. Suddenly, certain rights or obligations or restrictions assigned to or imposed on the contracting party become ineffective with respect to the consumer. This is directly indicated by the provisions of Article 381(1) and (2) of the Civil Code stipulating that such illegal clauses are not binding on the consumer, whereas the parties are nonetheless bound by the remaining provisions of the contract. The further legal effects of using abusive clauses are disputable (Bławat, Pasko, 2016). The created gap may be filled, if operative provisions can be found. Nevertheless, a problem is encountered when there are no such provisions. Directive 93/13/EEC in the recitals and in Article 6(1) as well as the case law of the CJEU indicate that the objective discouraging the entrepreneur to use illegal clauses is the contract continuation (Namysłowska, Skoczny, 2015: 19). When the quoted contact clauses are recognized as illegal, it will be difficult to supplement the legal relationship. This is permitted by the mutual will of both parties, however, in the absence of the consumer's will, attempts to change the regulations or the contract template are extremely difficult in view of a possible allegation that the quoted regulations are being circumvented with the aim to cause distress to the entrepreneur by applying such clauses (Namysłowska, Skoczny, 2015: 21). The right to amend the regulations when a legal relationship is in force may be exercised on condition that a precise modification clause is included in the regulations, and modification on the grounds of abusiveness, as well as the severability clause by reason of abusiveness would be disallowed (Namysłowska, Skoczny, 2015: 24). These would make it possible to circumvent the objective, namely the distress for the entrepreneur. In consequence, the conduct of bank resulting in, e.g., the inability to determine or change the amount of the performance, begins to destabilize hundreds and often thousands of loan agreements, and as a result, the bank may face a very serious problem, e.g. how to determine the amount of the cash performance which it is entitled to receive. A gap may have appeared in the method of determining the amount of the performance, which is difficult to replace. Similarly, the bank's right to change the interest rate, incorrectly formulated, may lead to the forfeiture of such right, although the market conditions will change significantly, which may be reflected in the bank's profitability. Another issue to mention to illustrate

the problem may be also the forfeiture of the contractual right to terminate the contract by the bank by reason of defective premises for making such a declaration of will which deteriorates the position of the bank as the creditor. The scale of the impact of such clauses with respect to the extended effectiveness of final decisions of the District Court, the Competition and Consumer Protection Court in Warsaw, is very extensive, covering all entities to which the contested normative content in the model of a specific entrepreneur applies (Supreme Court, III CZP 17/15). Similarly, the limits of the effectiveness of the decisions of the President of the Office of Competition and Consumer Protection (hereinafter: OCCP) are very wide (Competition and Consumer Protection Act, Article 23d). If abusiveness is detected, the refunding of overpaid amounts by consumers, the cost of publication of information, and the cost of remedying other effects of violations, may deteriorate the financial stability of the bank. Hence, an issue of a fundamental nature is to determine whether the bank will receive the assumed amounts arising from the executed contracts, or whether thousands of contracts, often high in value will bring the bank to the edge of stability, due to the unprofitability of such contracts when the contested provisions have been deleted. If the legal relationship is changed with respect to the economic conditions by eliminating the effectively contested provisions, most often it will be to the bank's disadvantage. Another type of risk involves the possibility of imposing a high cash fine (Competition and Consumer Protection Act, Article 106(1) (3a) in conjunction with Article 23a) as an ascertained violation of the prohibition to include illegal contractual clauses in contracts with consumers. It is very probable that a high cash fine will be imposed taking into account in particular: possible prior infringements of the provisions of the Act, actions conducted in order to earn profits, the scope of the benefit achieved, the extent of infringements, the degree of culpability. Cash penalties amounting event up to 10 % of the annual turnover per instance of violation could aggravate the problems of banks. Incidentally, it can be noted that the extent of social dissatisfaction arising from a sense of gross dishonesty suffered by consumers from banks may trigger political pressure and, as a result, reaction of the authorities that will take decisive action against banks, whether legislative in terms of introducing additional

costly obligations, propose new supervisory solutions, or even dare to interfere with the contents of the executed contracts. From the axiological point of view, the voice of an entity violating the elementary principles of integrity will be poorly perceived, even if it raises the right postulates, the attention and willingness to help will be with the party aggrieved by such actions. In consequence, subsequent risks for the operation of banks will be seen.

Actions violating consumer rights are accompanied by the question about the role and reaction of the supervisory authority in a situation of flagrant abuse of position by banks. The use of abusive clauses in this part of the financial market is a widespread and common practice, confirmed by valid court rulings, the conduct that is clearly assessed in a negative way. The existing two legal regimes which are supposed to ensure proper operation of the financial market in respect of transactions entered into with consumers, i.e. the competences and activities of the President of the OCCP as well as the competences and activities of the Polish Financial Supervision Authority are overlapping in certain areas. From the perspective of competence, the proper functioning of the financial market is to a certain extent the objective of both these institutions. The Polish Financial Supervision Authority (PFSA), *inter alia*, protects the financial market participants, and the President of the Office of Competition and Consumer Protection intends to protect the interests of consumers – a weaker group of entities in economic terms. As a result, the actions of both these institutions may significantly affect the form and condition of the financial market. It cannot be excluded that these activities will be carried out in opposite directions requiring that a balance is sought between punishing banks for gross violations of consumer rights and maintaining the stability and security of these institutions. Bearing in mind the vastness of problems for banks and for the financial market which are connected with finding abusive clauses in bank contracts, in particular those relating directly to the sphere of payment for bank services, a question arises whether it is possible to notice such risk and eliminate the factors that cause it. And specifically, whether the PFSA, supervising over the financial market, has the competences and tools for this purpose.

4 Competences of the Polish Financial Supervision Authority as the institution responsible for supervising the financial market

In the current legal status binding as of 1 January 2019 the Polish Financial Supervision Authority is a body of the Office of the Polish Financial Supervision Authority. The task of the PFSA includes but is not limited to supervision over the financial market entities, including banks, to ensure the stability of this market. As the competences of administrative authorities cannot be presumed, but should be defined (Zimmernann, 2018: 43), attention should be paid to the scope of tasks and powers of the PFSA from the perspective of the discussed issues. How are the limits of the PFSA's competences formed then with regard to the response to the violation of consumer rights by banks, in particular by introducing provisions violating consumer rights into the regulations, general terms of contracts and templates of contracts? The extent of regulations in the area of supervision over banks has been divided between the Financial Market Supervision Act and the Banking Law Act. As a consequence, it is necessary to analyze both these acts from the point of view of determining the possibility and possible scope of the PFSA's activities related to the response to the abusive clauses used by banks.

The Financial Market Supervision Act has empowered the Polish Financial Supervision Authority, *inter alia*, to supervise banks (Article 4(1) in conjunction with Article 1(2)) indicating the objectives of supervision and the generally defined tasks. Chapter 11 of the Banking Law contains further provisions relating to the supervision over banks. It explicitly stipulates the wide scope of objectives of the supervision over banks (Article 133(1) of the Act). It is intended to ensure the security of funds deposited on bank accounts and compliance with the banking law, the CRD IV Regulation, the National Bank of Poland Act, the decision on the licence to establish a bank, the statutes, and other referenced legal acts. On the other hand, the supervisory activities of the PFSA include, but are not limited to: assessing the compliance of credit facilities, cash loans, letters of credit, bank guarantees, sureties, issued bank securities with the regulations applicable

in this respect; assessing the financial condition of banks, including the quality of assets; assessment of the bank management system. In fact it is sufficient to notice this normative part of the supervisory authority's activity to answer the question about the scope and form of the PFSA's competence to assess loan agreements or cash loans in terms of lawfulness. A fundamental obligation of the PFSA has been to examine whether the granted credit facilities and loans comply with the applicable regulations which also means analysis from the point of view of the provisions of the Civil Code with regard to the existence of solutions suspected of being abusive in nature. Doubtlessly the PFSA has not had the competence to state in a binding way that the provisions of consumer contracts are illegal, nevertheless, analysis and assessment of the possible ineffectiveness of the flagrantly biased clauses in bank contracts should become the subject of evaluation. The non-binding nature of the illegal contractual provisions occurs by operation of law, it is binding on the *ex tunc* basis and the ascertainment of abusiveness is of a declaratory nature. Hence, it means that there was no need to wait for court decisions, or, as is currently the case, decisions of the President of the OCCP. The illegal nature of contractual clauses has been ascertained for many years, and this institution, and particularly the conditions for recognizing specific provisions as illegal, is supported by several thousand judgments, and the rich output of the doctrine. Hence, the understanding of this institution and its mechanisms has been established, and the interpretation of the key provisions of the civil code for the issue under consideration arouses no doubts as to the essential components thereof. It is generally known and understood which features of the model, under which conditions, and the date of assessment (Grochowski, 2019) determine its illegal nature. Furthermore, in Article 3853 of the Civil Code, the legislator has included examples of illegal contractual provisions which have been nevertheless used by banks, for example: making the rendering of the performance depend on circumstances depending on the consumer's contracting party's will; excluding or significantly limiting the contacting party's liability to the consumer for failing to perform or improperly performing an obligation; the consumer's contracting party's entitlement to unilaterally change the contract without a valid reason stipulated in such contract; providing

that it is only the consumer's contracting party that is entitled to unilaterally change the essential features of the performance without any valid reasons. It should not be a problem for an expert supervisor, whose duty is to ensure the proper functioning of the financial market, including the trust of entities that are the weaker parties in legal and financial relationships, to detect solutions proposed by banks that grossly violate the interests of consumers. Hence, the standpoint that the financial supervisor should not review the contents of contracts, terms and conditions of contracts, regulations used by the supervised bank but that it should only remain passive until the formal ascertainment of abusiveness of certain solutions should be considered as erroneous. It is impossible to implement the mentioned supervisory objectives if the principal activity of the supervised entity for which the licence was granted is not examined. Hence, ensuring the stability of the financial market should also mean analysis of the wording of documents intended to become a term or a condition of a contract, a contract template or regulations executed with consumers. Such supervisory analysis would allow eliminating the most dangerous exposures arising from preparing or attempting to apply solutions that could grossly violate consumer rights, both for the sake of stability of an individual bank and indirectly for the financial market. The mere risk of an illegal clause if it concerns a material issue or a content that has been repeatedly contested before, used even by institutions operating outside the financial market, should trigger a supervisory response. Such need is reinforced by the awareness that being in continuous contact with the supervised entities, knowing the specificity of the supervised part of the financial market and additionally employing highly qualified staff, the PFSA has all the instruments in place to carry out such analyses. Moreover, the speed with which the PFSA can become familiar with the proposed solutions and respond appropriately cannot be matched by any other public institution. It should be emphasized that the supervision exercised by the PFSA often takes the form of talks, peculiar negotiations with the supervised entities with the purpose to ensure the stability and correctness of the supervised activities, not just waiting for a bank's error in order to impose sanctions on the supervised entity. The argument that the PFSA is endeavouring to accomplish objectives that

are closer – related to a specific bank and its customers, and more distant ones – systemic objectives of supervision in a specific part of the financial market comprising the banking market, should resist the allegations, if any, questioning the PFSA's right to carry out such analyzes.

However, the problem of the lack of a proper response is more serious, as it questions the supervisory activities regarding the assessment of the bank's management system, in particular the risk management and internal control systems. In this respect, it should not be overlooked that, using the normative authorization, pursuant to Article138 (5) of the Banking Law the PFSA itself made the Recommendation M, relating to operational risk management in banks, understanding risk as a possibility of the occurrence of a loss resulting from non-compliance or unreliable internal processes in the bank, including also the legal risk. The risk related to a defective contract template has therefore been included among the internal risks. It was linked with the obligation to verify documents disclosed to the outside by a legal unit or a non-compliance unit or by external experts. In addition, the issue of mechanisms constructed in a defective way is pointed out in Annex 1 to Recommendation M where errors in contract templates or in the regulations are explicitly indicated among events posing risk. Hence, the issue of defective contractual provisions has been known and also described in the literature of the subject for a long time (Pisuliński, 2005).

The bank creates contract templates, terms and conditions of contracts, regulations, using the work of professional lawyers, who know not only the bank's expectations from the economic point of view of the offer but also the provisions of the law, including the necessity to take the requirements of consumer protection into account. Meanwhile, contractual clauses constituting explicitly flagrant violation of consumers' rights have been accepted and implemented under the bank and risk management systems. Risk management in banking operations has a fundamental dimension, and forming the contents of the legal relationship that obviously violates the consumer's rights cannot and could not be unnoticed by the supervisory authorities, whose statutory obligation consists in examining these issues.

Hence, there should be no doubts that the PFSA has had the competence to analyze the contents of contracts formulated in transactions with consumers, both from the point of view of the constitutional law and from the point of view of the banking law. What instruments could be considered then to obtain the effect of eliminating the provisions, even if only suspected of being blatant violations of consumers' rights, in bank contracts in the broad sense of the word.

The catalogue of measures that could be taken by the PFSA in response to the use of abusive clauses is extensive, though varies in time (Article 138 of the Banking Law). Supervising authority could offer recommendations to banks to develop and apply rules ensuring the proper functioning of the bank's management system, implementation of specific rules for creating provisions for risks related to the bank's operations, or reducing the risk inherent in the bank's operations. If the rules were not implemented, far-reaching consequences could follow, both personal for the president and members of the board of the bank, but also for the bank itself, starting from financial penalties, ending up with revoking the licence to establish the bank. Thus, there existed mechanisms at the disposal of the PFSA, both at the stage of detecting irregularities, making recommendations, deleting doubtful clauses and imposing sanctions, if the recommendations were not followed.

When considering the discussed issues, it should also be noted that pursuant to Article 138(7) of the Banking Law, measures taken during supervision shall not violate the contracts executed by the bank, expect for specifically indicated contracts. Nevertheless, the PFSA's ability to influence in the form of legal relationships already in place between banks and consumers should be distinguished from the influence on the form of the terms and conditions of contracts, contract templates, or regulations already forming or intended to form their basis. The process of supervisory examination and assessment of banks is continuous (Resolution of the Polish Financial Supervision Authority on the manner of exercising supervision over the banking activity, Section 10). This means that each statutory area of operation of these institutions is subject to continuous supervision. Thus, when irregularities are detected, specific supervisory response should be triggered, if the results

of such inspection and analysis raise justified concerns regarding the objective of ensuring the proper functioning of the financial market, its stability, security, and protection of the market participants. Since the scale of the banking operations in the consumer segment, i.e., both accepting deposits but also granting loans and credit facilities is significant, accordingly the scale of possible infringements may have severe consequences, which can, in extreme cases, destabilize the financial market.

5 Conclusion

The use of illegal clauses by banks in contracts leads to private and public law consequences, also exposing to the risk of possible reaction of the legislator to the observed conduct jeopardizing the financial stability of a large part of the society. The use of illegal clauses by banks may potentially cause serious risks not only for individual institutions but also for this part of the financial market. The scale of the effect of using illegal clauses in contracts on the stability of the banking sector varies. It fluctuates between formal breaches, in fact not causing any significant damage to consumers or banks, through provisions that may bring more severe consequences, to extremely risky clauses which may create strong tensions in the banking sector. The research objectives assuming the existence of the PFSA's powers to examine banking contracts in transactions with consumers in terms of their abusiveness have been confirmed. The applicable legal standards constitute not only the authorization for the PFSA to exercise such control but also the obligation accompanied by the powers to give recommendations and impose sanctions. Contracts that have been already concluded and contain abusive clauses pose a threat the full picture of which is not known and has not been estimated to date. The political initiatives undertaken[12] to take a closer look at the scale of banks' infringements against consumers can bring about much alarming information about the hidden scale of problems.

12 An example is the draft resolution of the Senate of the Republic of Poland calling on the Polish Financial Supervision Authority, the President of the Office of Competition and Consumer Protection and the General Prosecutor to eliminate loan contracts indexed in a foreign currency or denominated in a foreign currency containing illegal contractual clauses (print no. 218 of the current 9th term of office of the Senate) from legal transactions the in the Republic of Poland.

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Law and Innovations on the Financial Market

Witold Srokosz[1]

Abstract

This paper describes mutual relations between law and innovations in finance market, focusing on legal innovations consisting in regulating the financial institutions. Its goal it to confirm or debunk two hypotheses. The first one stipulates that degree and methods of legal regulation should be strictly correlated with the degree of development and popularization of a given financial innovation (especially with respect to technological innovations) and the risk connected with using it. The latter is related to the previous one and provides that it does not necessarily need to relate to legal innovations regulating new financial institutions. The legal dogma methods was used in this publication.

Keywords: Law; Business Law; Financial Market Regulation.

JEL Classification: K10; G21.

1 Introduction[2]

The goal of this paper is to identify mutual relations between law and innovations on the finance market, focusing on legal innovations consisting in regulating the financial institutions. Legal regulations may support the development of a given financial innovation, limit it or be neutral for its development, with the effect of applying law not always corresponding to the intentions of law-makers. In this work we put forward a hypothesis that degree and methods of legal regulation should be strictly correlated with the degree of development and popularization of a given financial innovation and the risks connected with using it. In particular, we put forward

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a hypothesis that there is little use in extensive development of regulations ahead of time, with the law-maker forecasting development trends and setting an ambitious goal of drafting regulations that will efficiently respond to the financial innovations in the future (especially with respect to technical innovations) that were still not popular at the moment of drafting these regulations or even existed just in its conceptual phase. However, this is far from evident in the case of legal innovations regulating new finance institutions. The legal dogma methods was used in this publication.

2 Types of financial innovations from the perspective of finance system

As often noted in the literature "finance is nothing more than a long chain of innovations leading to development of novel financial products and processes used to improve allocation of capital and risk management". (Avgoluleas, 2014: 1–2) Each of the solutions applied at finance market was an innovation back at some moment. "Novelty" is the immanent feature of innovation and the very notion of innovation is relative. Therefore, time framework should always be provided when talking about innovations.

Financial innovations are defined and used mostly in economics. However, there is no universally accepted definition of financial innovation, or even a single approach. It seems that it would thus be better to use such a definition that can be best used to achieve the goal set. Thus, for investigations in this paper we accepted such an understanding of financial innovation that remains closely related to the notion of finance system. From this perspective, the notion of financial innovation is mostly used in its narrow meaning covering new solutions in financial instruments (completely new instruments, combinations of a couple of traditional instruments, new applications of existing instruments, new financial techniques, new finance services etc.). Financial innovations can also be defined in a broader perspective as new solutions in any element of the finance system (within markets, instrument institutions, financial operations and regulations) [Marcinkowska, 2012: 76]. Such a perspective should be expanded with such an element of the finance system as money because new financial innovations can also relate to money.

Table 1 presents types of financial innovations in the broader understanding, together with examples.

Elements of the financial system	Types of financial innovations	Examples of financial innovations
Financial institutions	New forms and types of financial institutions	payment institutions, electronic money institutions, cryptocurrency exchanges,
Financial markets	New segments of the financial market	derivatives market, "market for cryptocurrencies and tokens"
Financial instruments	New financial products and services(financial innovations in the narrow perspective)	securitization, physically settled comodity derivatives, inverted mortgage, some types of tokens
Infrastructure	New infrastructural solutions	multilateral trading facility (MTF), cryptocurrency systems, Etherium and similar systems (on which smart contracts work)
Money	New types	cryptocurrencies, virtual currencies
Regulations	New legal regulations	new regulations on capital adequacy (eg risk assessment principles); blockchain technology first develops and only then legal regulations are created

Drafted on the basis of (Marcinkowska, 2012: 74).

Moreover, technological innovations such a cryptocurrencies or the blockchain technology should also be distinguished among financial innovations. On the other hand, OECD classification distinguishes such innovation types as: product, process, marketing and organizational innovations, with financial innovations usually being of mixed character i.e. product-process, product-marketing, marketing-process, or product-process-organizational (Marcinkowska, 2012: 85).

In the finance market the so-called FinTechs[3] are strictly related to financial innovations.

3 Need for legal regularization of financial innovations

Financial innovation lead to the development of finance markets but experiences from history, especially the lesson learned from the world 2007 crisis, clearly show that especially due to the progressing globalization, financial innovations may threaten the stability of these markets, lead to bankruptcy of financial institutions and losses among customers, especially consumers (see for example: Beck, 2016: 28).

Examples of such an financial innovation, co-responsible for the last world financial crisis, includes securitization understood here as "*the transfer of packages of bank loans, especially mortgages, to free-standing 'special investment vehicles', which issued securities that were then sold to investors*" (Armour, 2016: 7). It is a mixed-type innovation, difficult to classify, being a combination of "traditional" financial instruments with a new type of financial institution.

Legislators in the US responded to the 2007 crisis with the Dodd Frank Act, and in Europe with a series of directives: EU Capital Requirements Directive (CRD IV) and the Capital Requirements Regulation (CRR), the European Markets Infrastructure Regulation (EMIR), MiFID II and the Market in Financial Instruments Regulation (MiFIR). These regulations mostly relate to financial innovations, equally to securitization as to shadow banking[4], technological innovations e.g. algorithmic trading and HFT[5] to new innovative financial instruments such as e.g. physically settled commodity

3 There is no legal definition of FinTechs. The doctrine rightly avoid construing a definition of FinTech; description of activities connected with FinTech dominates (Szpringer, 2017: 3). However, some authors, after carrying out extensive research on scientific publications concerning FinTech, suggest comprehensive understanding of fintech, as innovative companies active in the financial industry making use of the availability of communication, the ubiquity of the internet, and the automated processing of information (Milian, 2019: 1, 18).

4 Shadow banking is also considered a financial innovation (Avgoluleas, 2014: 8; J. K. Solarz, 2014: 214–215; Nesvetailova, 2014: 431–440). Securitization constitutes one of the significant elements of shadow banking, but not the only one as it also covers e.g. repurchase agreements – repos, Hedge Funds or Mutual Funds (see more: Girsa, 2016: 47 ff).

5 Both algorithmic trading and high-frequency trading (HFT) are subject to specific rules in MiFiD II (see more Bush, 2017: 469 ff).

derivatives. On the basis of these regulations we may point that the reasons behind legal regulations of financial innovations in the EU is to guarantee financial stability of the uniform financial market, solvency and liquidity of financial institutions and protection of investors' interest, including mostly consumers. The EU legislator intends to achieve it by expanding, making more precise and standardizing prudence norms in the whole EU (with CRR being an example), expanding the scope of limitations (e.g. by expanding the catalogue of financial instruments), expanding on information and reporting duties. After the 2007 crisis common finance supervision system was created in the EU (with Single Supervisory Mechanism (SSM) in Eurozone[6]). Guidelines issued by European financial supervision bodies as soft law significantly complement legal regulations on financial innovations. In specific member states supervision bodies issue acts qualified as soft law (e.g. in Poland these include supervision boards, Financial Supervision Authority gives recommendations).

Regulations on money laundering and counteracting financial terrorism constitute a significant regulatory area relating to finance market. The fourth AML Directive has recently been amended with AML V Directive and one of the most important goals of this amendment was to include exchange of virtual currencies into legally accepted monies in its coverage and to recognize cryptocurrency exchange offices as obliged entities.

There is also a need to regulation of financial innovations in tax law. Individual member states take appropriate legislative actions with respect to income (revenue) taxes. For example in Poland, at the beginning of 2019 legal regulations on subjecting incomes from selling cryptocurrencies to personal income tax entered into force. Earlier, incomes from paid sales of financial instruments has been gradually covered by regulations.

4 Legal regulations on financial instruments as financial innovations

From the economic perspective financial instruments are assets that can be traded. They can also be seen as packages of capital that may be traded (Investopedia.com). According to Oxford Dictionary of Finance and

6 About SSM and European Union Banking see more Bush, 2015: 95 ff.

Banking a financial instrument is a contract involving a financial obligation (Smullen, 2005: 154). Thus, financial instruments are agreements to exchange something of value in return for something of value (Rechtschaffen, 214: 49). However, there is a discrepancy between such an economic take and the legal take: it is not always the case that something classified as financial instrument in the economic perspective is also an instrument in the legal perspective. In particular, such discrepancies can be observed with respect to financial innovations. Very often new financial instruments are difficult for unambiguous legal classification as it is for example the case with tokens issued on the basis of smart contracts and operating on blockchain (the most popular tokens are issued with the use of smart contracts in the Etherium network in the ERC20 standard. Their classification depends on the actual financial conditions and white paper provisions as well as the regulation on the basis of which they are issued (if such regulations exist). These tokens that are only a medium of payment definitely will not be regarded as financial instruments within the understanding of MiFID II. Significant doubts may arise in the case of security tokens and investment tokens. Thus, appropriate legal regulation concerning token at EU level is advocated (draft report on the proposal for a regulation of the European Parliament and of the Council on European Crowdfunding Service Providers). A similar scheme kept repeating: a new financial instrument emerged and then the EU legislator, followed by individual member states, introduced appropriate regulations. The last example includes recognizing *physically settled commodity derivatives* as financial instruments in EU law. This was done by including, in point 6, section C of Appendix I (this section includes a list of financial instruments) to the MiFID II Directive, "*derivative contracts relating to goods that can be physically settled*" on certain conditions covered in this point.[7]

7 This point takes the following wording: "Option transaction, future-type transactions, swaps and any other derivative contracts relating to goods that can be physically settled on condition that they are subject to trade on regulated market, MTF or OTF, to the exception of power industry products sold wholesale, being the object of OTF trade that need to be physically settled".

5 Legal regulations for financial innovations in their broad understanding with special attention to regulations of new financial institutions

Generally, rationing scheme consists in providing specific financial services (performance of specific activities or running a specific finance business) being not allowed for anybody, but limited to the entities defined in law once the conditions provided for therein are met. This is achieved with a ban supported by appropriate sanctions. In this way, provision of banking services was regulated in the CRD IV Directive (see art. 8, art. 9 and art. 66.1. a) or provision of payment services in the PSD II Directive (see art. 11, art. 37.1, art. 103). Technological innovations connected with product-process-organization innovations can significantly change the form of traditional finance services what was recently the case for payment services. In this area it was the revolution initiated by the PayPal company that has led to a necessity of drafting comprehensive regulations on provisions of payment services, which was done in the EU with the PSD Directive. First, entities providing the new payment services kept developing dynamically and with the PSD Directive the EU legislator regulated operation of these entities, thus providing regulations for the new finance institution – payment institution.[8] Further intense changes in provisions of such services (e.g. emergence of the new service granting access to information on account or development of payment initiation services consisting in establishing a software interface between the webpage of the acceptor and Internet banking platform of the payment service provider who operates payer's account for the purpose of initiating payments done via the Internet based on transfer order) brought about the necessity of amending the PSD Directive and passing a new PSD II Directive. We still observe intense, innovative changes in provision of payment services, which can be best exemplified with emergences of the cryptocurrency systems which are not covered

8 EU legislator provided for some exceptions that member state could use to pose less strict conditions for starting and running business in some payment services. Polish legislator used this opportunity and apart from payment institution, the payment services act also provides for a payment service office as an entity that might exclusively provide money transfer services within the territory of Poland and such business can be run by a natural person. Payment service offices have become quite popular in Poland (since 2018 there were ca. 1400 of them).

by the PSD II Directive. This gives rise to a question on the need for regulating operation of such systems at least for the purpose of consumer protection. This directive constitutes a natural place for a definition of virtual currencies (preferably with distinction of cryptocurrencies). As for today such a definition can be found in AML IV Directive amended with AML V.

Cryptocurrency systems are just one of the methods of using the blockchain technology and one of the examples for the development of the so-called FinTechs that are based on technological innovations and exert increasingly strong influence on the shape of the finance market. The German BaFin (Federal Financial Supervisory Authority) made a list of business models that can be qualified as FinTech businesses. These are the following business models (BaFin, 2019):

- alternative payment methods,
- automated portfolio management,
- blockchain technology,
- crowdfunding (including crowdinvesting and crowdlending),
- platform for automated investment advice,
- platform for signal trading and automated order execution,
- Virtual Currency (VC),
- insurtech companies.

Some of these innovative solutions are subject to currently binding provisions of law providing for specific limitations as it can for example be the case for emissions of investment or share token that can be subject to MiFID II regulations. Generally sooner or later it will become possible to create appropriate provisions in public and consumer law. What needs to borne in mind is that in the case of financial innovations based on technological innovations, i.e. undoubtedly the majority of FinTechs, it makes little sense to create legal provisions upfront, and even less so to make such provisions that would force technological progress in a given area. The best example includes the 2009/110/EC directive on electronic money that was ruled when the subject of regulations was not popular but only expected

to get popular soon.[9] Unfortunately, this is not the case till date. Other, alternative payment methods developed that are currently subject to regulation in PSD and PSD II directive, and virtual currencies keep developing right now. Even slackening prudence norms relating to electronic money and shifting the regime applicable to credit institutions to prudence regime applicable to payment institutions did not help to popularize electronic money.[10]

In Poland an attempt to create a financial institution in 1997 i.e. a savings and building society with status of a bank in the form of a corporation ended in a similar fiasco. The 05 June 1997 act was a response to this situation (The Act on Savings and Building Societies)[11], but in the following years still not a single such society was created (which means that none of the banks received appropriate permit of the Bank Supervision Authority) and as a result the law was repealed on 31 December 2001.[12] Regulation of the savings and building society was not the result of applying technical or any other innovations, as such institutions did not exist before 1997 in the unregulated sphere. Similarly, electronic money was not used in practice before passing the 2009/110/EC Directive. Meanwhile, before passing the PSD Directive, numerous institutions providing innovative payment services have been running their business without any regulations. Thus, legal regulation of construction credit unions was only an innovation in law, relating to norms and regulations. I was thus similar to regulating electronic money, which was also a legal innovation, but at least this one was based

9 Electronic money means electronically, including magnetically, stored monetary value as represented by a claim on the issuer which is issued on receipt of funds for the purpose of making payment transactions as defined in PSD II, and which is accepted by a natural or legal person other than the electronic money issuer.

10 For example in Poland not a single permit has been issued so far, so there is not a single electronic money institution with its office in Poland. Whereas in Europe, there are 172 electronic money institutions (Report on the implementation and impact of Directive 2009/110/EC).

11 In line with art. 2 of this act, without prejudice to art. 5.2, society activities only included accepting saving account balances from natural persons to individual target accounts and granting them loans for residential purposes. In line with art. 5.2 the unions could temporarily invest free resources: 1) in securities issued by the Treasury or National Bank of Poland, 2) in fixed-term deposits in banks.

12 It was repealed with the Act amendments to Bank Warranty Fund, Energy Law, Political Parties and other Laws.

on a technological innovation and related to money (I mean electronic money), even though it was not popular at the moment the 2009/110/EC Directive was passed and entered into force.

These examples show that it only makes sense to create new financial institutions in legal regulations when in practice there are already entrepreneurs running such business activities and these are not subject to regulations yet. Therefore, it seems that it would be better to create new communal credit institutions[13] in Poland, with a new legal regulation based on already existing self-government financial institutions, such as self-government guarantee funds[14] or self-government loan funds[15]. Such funds have been operating in Poland for years without any special legal regulations.

6 Conclusion

The reasoning conducted in this work confirms our hypothesis that degree and methods of legal regulation should be strictly correlated with the degree of development and popularization of a given financial innovation and the risks connected with using it. We also managed to confirm the hypothesis that it makes little sense to go ahead of practice and provide legal regulations for financial innovations (especially technological innovations) that have not yet become popular. Such a conclusion also pertains to regulating new financial institutions. Entities already engaging in trade should rather

13 What is meant here is a reference to the notion of credit institution within the understanding of the CRR Regulation. In the doctrine and in practice there is no common definition of communal credit institution. In this paper this notion is used in a narrower sense, as it is limited to entities meeting the pre-conditions for the definitions of EU loan institutions that are totally and partially owned by local self-government unit and possibly controlled by these entities. Right now, in Poland there are practically no communal credit institutions within this understanding (by means of an exception some communes have shares in cooperative banks, but such cases are rare). There is also no separate, comprehensive legal regulation allowing for creation of such institutions. There only exists a fragmentary and practically unused legal regulation in art. 10.3 the Act on Municipal Economy.

14 Regional development funds (commercial law companies) established by the voivodship on the basis of art. 13 (1a) The Act on the Voivodship Self-government, which provide loans or guarantees to local entrepreneurs (because of their communal character they may also be called self-government loan funds).

15 Self-government guarantee funds are commercial law companies established by territorial self-government units pursuant to art. 2 The Act on Municipal Economy in the sphere of public utilities, which only provide sureties to local entrepreneurs.

be covered by regulations instead of creating at legal level possibilities for the entrepreneurs to engage in specific, still unpopular financial activities.

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The Nature of Legal Relationships between Financial Safety Net Bodies Based on the Example of the Planning of Forced Restructuring of Banks

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Abstract

This contribution concerns the issue of the development, review and feasibility assessment, as well as updating plans of forced restructuring of banks. The drawing up of plans by the Bank Guarantee Fund is carried out in cooperation with financial safety net bodies. The main scientific objective of this contribution is to analyse and evaluate the juridical effectiveness of the regulations governing legal relations between financial safety net authorities at the planning phase of forced restructuring of domestic banks. This has allowed showing that the system of powers and responsibilities which form the basis for cooperation in the planning of forced restructuring is inefficient in terms of timing and does not con-tribute to harmonising the activities of the financial safety net authorities.

Keywords: Financial Safety Net; Forced Restructuring; Restructuring Plans; Financial Supervision.

JEL Classification: G28; K23.

1 Introduction

The development, review and feasibility assessment, as well as updating plans of forced restructuring of banks is the responsibility of the Bank Guarantee Fund[2]. Not only does the planning affect the proceedings on forced restructuring but also has an impact on current operations of the banks.

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2 Forced restructuring is also referred as special resolution regime.

This is so because the planning of forced restructuring is related to banking activities. Plans of forced restructuring concern each domestic bank separately, irrespective of its financial situation. The Bank Guarantee Fund draws up both individual plans for forced restructuring of domestic banks and group plans for banking groups and institutional protection systems for cooperative banks. The drawing up of plans by the Bank Guarantee Fund is carried out in cooperation with the Polish Financial Supervision Authority, the National Bank of Poland, the minister responsible for financial institutions or the Financial Stability Committee. Thus, it is important to regulate the legal relations between bodies within the financial safety net (Campbell, Lastra, 2010: 162–170; Jurkowska-Zeidler, 2017: 390; Zawadzka, 2017: 40–44; Colliard, 2019).

Due to the impact of forced restructuring planning on the on-going activities of banks, the crucial issue for the determination of legal relations is the cooperation between the Bank Guarantee Fund and the body for the supervision of domestic banks, i.e. the Polish Financial Supervision Authority. However, performing the responsibilities of a similar nature by the Bank Guarantee Fund and the Polish Financial Supervision Authority may cause difficulties in the distribution of responsibilities and the impact of decisions taken by those authorities on operations of banks.

This study is to analyse and evaluate the juridical effectiveness of the regulations governing legal relations between financial safety net bodies at the planning phase of forced restructuring of domestic banks. This has allowed showing that the system of powers and responsibilities which form the basis for cooperation in the planning of forced restructuring is inefficient in terms of timing and does not contribute to harmonising the activities of the financial safety net authorities. The topicality of the issue in question is related to the proposed legislative amendments aimed at streamlining and accelerating the process of adopting and updating forced restructuring plans[3].

[3] This regards the draft act of 7 September 2018 on the amendment of the Act of 10 June 2016 on the Bank Guarantee Fund, deposit guarantee scheme and forced restructuring (Sejm Papers no. 2877), hereinafter: "the draft Act on the amendment of the Act on the Bank Guarantee Fund".

2 The obligation of preparing forced bank restructuring plans and their structure

The development of restructuring plans constitutes a kind of foundation for the whole process of forced restructuring of a bank[4]. The due performance of obligations related to the planning of forced restructuring may prevent banks from bankruptcy (Szczęśniak, 2018: 27). In view of the above, plans for forced restructuring of banks are sometimes referred to as "living wills" (Avgouleas, Goodhart, Schoenmaker, 2012: 210; Guynn, 2013: 109). Subsequent review and feasibility assessment, as well as an update of forced restructuring plans, strengthen the financial standing of banks. By performing these obligations, banks can become more credible for other financial market participants. Plans for forced restructuring also limit the risk of operations by improving the capital adequacy and liquidity of banks. As a consequence, the planning of forced restructuring of banks increases the level of protection of stability of the domestic financial system (Lastra, Wood, 2010: 531; Schollig, 2013: 17).

According to Article 73 paragraph 1 of the Act on the Bank Guarantee Fund (ABGF), the plan is to be developed in a view to arranging a forced restructuring of a domestic bank. Forced restructuring plans are to be developed for domestic banks that are not part of a group subject to consolidated supervision in another EU Member State. The preparation of plans allows for conducting forced restructuring of the bank. Therefore, it is impossible to implement the objectives of forced restructuring without performing the obligations in this regard (Huertas, 2013: 167). This is so since the Bank Guarantee Fund, as set out in the provision of Article 67 paragraph 1 item 1 ABGF, meets these objectives by drawing up forced restructuring plans. The Bank Guarantee Fund has the obligation to develop both individual plans of forced restructuring for domestic banks and group plans for institutional protection systems for cooperative banks (ABGF, Art. 96/1). Moreover, the Bank Guarantee Fund is required to develop a group plan of forced restructuring for the group of a domestic parent entity, in which at least one subsidiary is located in a Member State other than the Republic of Poland (ABGF, Art. 74/1).

4 According to recital 25 of the BRR Directive, resolution planning is an essential component of effective resolution. Authorities should have all the information necessary in order to identify and ensure the continuance of critical functions.

The scope of the Bank Guarantee Fund's powers with regard to a bank facing the risk of bankruptcy is limited by the previously devised plan of forced restructuring of the bank. This is so, because the plan outlines possible variants and strategies for conducting forced restructuring. It should be adapted to possible crisis scenarios. The content and elements of the forced restructuring plan are listed in the provision of Article 81 paragraph 1 ABGF. According to this provision, a plan of forced restructuring consists of two parts. The first part is a description of planned activities *vis-a-vis* the bank in the event forced restructuring is initiated. The second part of the plan comprises an assessment of the feasibility of these activities.

3 Nature of legal relationships between bodies of financial safety net at the stage of development and adoption of plans for forced restructuring of banks

The obligation to develop forced restructuring plans is within the responsibility of the Bank Guarantee Fund (ABGF, Art. 73/1). The development of forced restructuring plans is not possible without cooperation with the Polish Financial Supervision Authority and the National Bank of Poland. For the stage of development of forced restructuring plans the legislature has used a form of cooperation of an actual nature (Biernat, 1979: 80). The activities of authorities working with the Bank Guarantee Fund do not result in the establishment, amendment or expiry of a legal relationship. The very development of forced restructuring plans, pursuant to the provision of Article 78 paragraph 1 ABGF shall be carried out in particular based on information obtained from the Polish Financial Supervision Authority and domestic banks. The minister responsible for financial institutions, acting upon the authorisation referred to in Article 87 ABGF, defined by regulation the detailed scope, procedure and time limit for the notification to the Fund of the information necessary to develop, update and evaluate the feasibility of forced restructuring plans[5]. The Bank Guarantee

5 Regulation of the Minister of Development and Finance of 25 May 2017 on the information necessary to develop, update and evaluate the feasibility of forced restructuring plans and group plans for forced restructuring (Journal of Laws of 2017, item 1080).

Fund, according to § 3 of the said regulation, is entitled to obtain information from the above-mentioned entities regarding, inter alia, the scope of the licence for running their activities and the activity actually performed, the equity and organisational structure, as well as the critical and major business lines. The Polish Financial Supervision Authority and domestic banks are required to provide the Bank Guarantee Fund with the information necessary for the development of forced restructuring plans. The due exchange of information shall ensure that the equity and organisational structure of the banks and the scope of their activities and respective risks are known. As the internal structures of banks must be known, the lawmakers have provided the Bank Guarantee Fund with access to the necessary information for the development of forced restructuring plans.

To perform the obligation discussed herein, the Bank Guarantee Fund may also use the information to be provided by other public administration authorities. The Bank Guarantee Fund is entitled to a claim against those authorities. An example of this may be information obtained from the National Bank of Poland. This is so because, pursuant to the provision of Article 81 paragraph 1 item 10 ABGF, a forced restructuring plan should comprise an analysis of the possibility of using the standard instruments of the National Bank of Poland to support liquidity of the entity concerned. The plan should also specify the domestic bank's assets which may constitute a security for such support (ABGF, Art. 81/4) Moreover, the forced restructuring plan can provide for a support for the bank's liquidity by the National Bank of Poland. The assistance may not differ from the terms generally accepted by the central bank, in particular as regards the time limit, interest rates and forms of security. Otherwise, the support from the National Bank of Poland would be contrary to the prohibition of exceptional support from public funds (Fernandes, Farinha, Martins, Mateus, 2016: 707; Panfil, 2017: 418; Amorello, 2018: 397).

A forced restructuring plan should be adopted in the form of a resolution to be taken by the Management Board of the Bank Guarantee Fund. This resolution must be communicated to the Polish Financial Supervision Authority and to the Minister competent for financial institutions. Before adopting the resolution, the Bank Guarantee Fund must, pursuant

to the provision of Article 73 paragraph 1 ABGF to consult the Polish Financial Supervision Authority about the assessment of the draft forced restructuring plan. However, the Bank Guarantee Fund is not legally bound by a statement of the consulted authority. On the other hand, the opinion of the Polish Financial Supervision Authority may be an element allowing proper determination of the legal situation in the proceedings for the adoption of a forced restructuring plan and may affect the decision of the Bank Guarantee Fund. Nonetheless, the content of the opinion on the assessment of the forced restructuring draft plan, does not constitute legal evidence. The opinion of the Polish Financial Supervision Authority is not to demonstrate whether certain facts exist or not, but rather to legally assess facts that have already been established.

The forced restructuring plan must be adopted by the Bank Guarantee Fund within its administrative discretion. In view of the above, the legislature does not specify what criteria are to be adhered to by the Polish Financial Supervisory Authority when issuing the opinion. The plan, as indicated in Article 73 paragraph 1 ABGF, is intended as a basis for forced restructuring. It should be assumed that a statement of the consulted authority should take into account the objectives of the supervisory authority's activities and the objectives of forced restructuring.

However, pursuant to Article 11 paragraph 5 ABGF, the provisions of the Code of Administrative Procedure shall not apply to the resolution on the adoption of a forced restructuring plan. The legislature clearly excludes resolutions for the adoption of a forced restructuring plan from the category of administrative decisions. From the point of view of the Bank Guarantee Fund, this means that the resolution is a non-sovereign form of activity (Iserzon, 1968: 77). Therefore, this also waives the applicability of Article 106 § 1 of the Code of Administrative Procedure, which defines the legal relations between public authorities. According to this law, if a provision of law makes the issue of a decision dependant on a position being taken by another authority (i.e. expressing an opinion or consent, or expressing a position in some other form) then the decision shall be issued once the position has been taken by that authority. The authority requested for an opinion must present it, in the form of an order, without

delay but no later than within two weeks from the date of service of the request, unless applicable law provides for another time limit.

Thus, the possibility of adopting a resolution to adopt a forced restructuring plan is not conditional upon failure to obtain the opinion from the Polish Financial Supervision Authority. Therefore, the statement given by an advisory body does not create a new legal relationship. The Bank Guarantee Fund is therefore entitled to rely on its own actual and legal findings, independent of the position of the Polish Financial Supervision Authority. It cannot be claimed under Article 73 paragraph 1 ABGF that the Bank Guarantee Fund is obliged to suspend the procedure for forced restructuring plan in view of the need to obtain an opinion from the Polish Financial Supervision Authority. Also, the Bank Guarantee Fund is not entitled to submit a request for expediting the proceedings or to file with an administrative court a petition for that authority's failure to act or excessive length of proceedings. The opinion in question is not of a precedent nature. Consequently, the absence of the position of the advisory body will not constitute a basis for the resumption of proceedings.

The waiver of application of the provisions of the Code of Administrative Procedure to the decision on the adoption of forced restructuring plans does not eliminate the need to set a time limit for the issuance of the opinion by the Polish Financial Supervision Authority. Whereas, under the currently applicable law, no time limit is specified in the Act on the Bank Guarantee Fund, which forms the legal basis for the procedure for adopting a forced restructuring plan. For this reason, the draft act amending the above-mentioned law sets a time frame for the expression of opinion by the supervisory authority. In accordance with Article 1 item 10 of the draft Act on the amendment of the Act on the Bank Guarantee Fund, the Polish Financial Supervision Authority will be required to express an opinion on the assessment of the forced restructuring draft plan within thirty days of the date of service of the draft plan by the Fund[6]. The determination of the time limit for expressing position by the supervisory authority will provide a formal condition for the common action in development and adoption of plans for forced restructuring.

6 Cf. Article 1 item 10 of the Draft act on the amendment of the Act on the Bank Guarantee Fund, p. 5.

4 Nature of legal relationships between bodies of financial safety net at the stage of feasibility assessment and update of plans for forced restructuring of banks

The Bank Guarantee Fund has also further responsibilities regarding the planning of forced restructuring. This authority is obliged to review and assess the feasibility of the plans and to update them. The first assessment of the feasibility of forced restructuring plans is made by the Bank Guarantee Fund at the stage of their development (ABGF, Art. 89/1).

Then, a review and evaluation of feasibility of the plans is carried out at least once a year. When assessing the impact that bankruptcy of a domestic bank could have on the financial situation, the Fund's Council is entitled to consult the Financial Stability Committee. Consequently, this opinion is not binding for the Bank Guarantee Fund. The opinion is to be issued on the basis of a draft resolution of the Bank Guarantee Fund. Before preparing the opinion, the Financial Stability Committee should be first allowed to get acquainted with the content of the proposed resolution.

After a significant organisational or legal change in the bank, the Fund evaluates feasibility of the forced restructuring plan. Then the feasibility assessment allows, if necessary, for an update of the forced restructuring plan. The Management Board of the Fund updates the plan of forced restructuring by way of a resolution (ABGF, Art. 91/1). During the feasibility assessment and updating of the plan, the Bank Guarantee Fund is obliged to consult the Polish Financial Supervision Authority.

However, pursuant to Article 11 paragraph 5 ABGF, the provisions of the Code of Administrative Procedure shall not apply to the resolution on update of a forced restructuring plan. The legislature, as in the case of resolutions on adopting plans of forced restructuring, clearly excludes resolutions on the updating of these plansfrom the category of administrative decisions. Therefore, this also waives the applicability of Article 106 § 1 of the Code of Administrative Procedure, which makes the issuance of the decision conditional on another authority's opinion. Thus, the possibility of updating a resolution to adopt a forced restructuring plan

is not affected by failure to obtain an opinion from the Polish Financial Supervision Authority. Therefore, the statement given by an advisory body does not create a new legal relationship. The Bank Guarantee Fund is therefore entitled to rely on its own actual and legal findings, independent of the position of the Polish Financial Supervision Authority. It cannot be claimed under Article 91 paragraph 1 ABGF that the Bank Guarantee Fund is obliged to suspend the procedure for updating a forced restructuring plan in view of the need to obtain an opinion from the Polish Financial Supervision Authority. The opinion in question is not of a precedent nature. Consequently, the absence of the position of the advisory body will not constitute a basis for the resumption of proceedings.

The waiver of application of the provisions of the Administrative Code to resolutions on updating forced restructuring plans, as in the case of resolutions for the adoption of these plans, indicates the need to set a time limit for the issuance of an opinion by the Polish Financial Supervision Authority. Whereas, under the currently applicable law, no time limit is specified in the Act on the Bank Guarantee Fund, which forms the legal basis for the procedure for updating a forced restructuring plan. For this reason, the draft act amending the Act on the Bank Guarantee Fund sets a time frame for the expression of opinion by the supervisory authority. Pursuant to Article 1 item 14 point a) of the draft Act on the amendment of the Act on the Bank Guarantee Fund, the Polish Financial Supervision Authority will be required to express an opinion on the assessment of the update of forced restructuring plan within thirty days of the date of service of the draft update of the plan by the Fund[7]. The determination of the time limit for expressing position by the supervisory authority will provide a formal condition for the common action during the update of plans for forced restructuring.

In the event any circumstances occur that prevent or impede the conduct of forced restructuring, the implementation of the obligations to develop and adopt the plan and update are to be suspended until necessary measures to remedy those circumstances are identified. If such circumstances

7 Cf. Article 1 item 14 point a) of the Draft act on the amendment of the Act on the Bank Guarantee Fund, p. 6.

are found, the Bank Guarantee Fund must notify in writing the domestic bank concerned and the Polish Financial Supervision Authority (ABGF, Art. 91/4). Then the domestic bank, pursuant to Article 91 paragraph 5 ABGF, is obliged to draw up an action plan to remedy these circumstances. This plan is to be submitted to the Bank Guarantee Fund within four months of the date of becoming aware of the circumstances which prevent or impede the conduct of forced restructuring. The Bank Guarantee Fund assesses the proposed plan and sets the measures necessary to remedy these circumstances. The decision on the determination of the measures in question shall be taken in the form of a resolution of the Management Board of the Bank Guarantee Fund, to which the provisions of the Code of Administrative Procedure are applicable. The resolution in question has the character of administrative decision. This means that the Bank Guarantee Fund is entitled to form rights and obligations of banks in a sovereign manner.

If the bank does not cooperate as regards drafting of the plan, or otherwise prevents its development, the Bank Guarantee Fund may issue an administrative decision on determination of measures to remedy such action. The Bank Guarantee Fund, when deciding on the determination of the measures necessary to remedy circumstances which prevent or impede the conduct of forced restructuring, is obliged to consult the Polish Financial Supervision Authority (ABGF, Art. 91/7).

In view of the fact that the decision on the measures necessary for remedying circumstances which prevent or impede the conduct of forced restructuring is taken in the form of an administrative decision, Article 106 § 1 of the Code of Administrative procedure 6 applies. However, the decision on the said measures may be issued only after the opinion-giving authority expresses its position. The Polish Financial Supervision Authority has the right to carry out clarification proceedings. A position of the consultative authority must be taken by way of an order. Therefore, a statement given by the consultative authority does not create a new legal relationship. Thus, an opinion of the Polish Financial Supervision Authority does not have the character of a precedent As a consequence, the Bank Guarantee Fund is entitled to submit a request for expediting the proceedings or to file with an administrative

court a petition for that authority's failure to act or excessive length of proceedings conducted by this authority. Where the decision is issued by the Bank Guarantee Fund without prior obtaining of the required position of the consultative body, this will form a basis to resume the proceedings.

However, the content of the opinion is not binding on the Bank Guarantee Fund. The opinion may become an element of the procedural material in a broad sense in the proceedings for measures necessary to remedy circumstances which prevent or impede the conduct of forced restructuring and, to affect the decision of the Fund. Nonetheless, the content of the opinion on the assessment of use of the measures concerned does not constitute legal evidence[8]. The opinion of the Polish Financial Supervision Authority is not to demonstrate whether certain facts exist or not, but rather to assess, in legal terms, facts that have already been established. The opinion in question, like the opinion on the assessment of the forced restructuring draft plan, is therefore the result of a syllogistic inference.

The bank may appeal against the decision. According to Article 106 § 3 of the Code of Administrative Procedure, the Polish Financial Supervision Authority should express its opinion without undue delay, however not later than within two weeks from the date of service of the request. The draft Act on amending the Act on the Bank Guarantee Fund extends this time limit to thirty days[9]. As it can be seen, the proposed solution will not streamline the process of forced restructuring, contrary to the intentions of the authors of the draft act[10]. Moreover, the Bank Guarantee Fund is entitled

8 It is widely accepted in the scholarly literature on the subject, not always correctly, that the position of the co-operating body in accordance with Article 106 § 1 of the Code of Administrative Procedure may always serve as evidence material. Some authors state that the content of the co-operating body's position is part of the evidence taken into account in the selection of the appropriate decision in a particular case. It should be noted, however, that an opinion which aims to assess the law for a particular factual state may become evidence as a document indicating whether the body has failed to act or not.

9 Cf. Article 1 item 14 point c) of the Draft act on the amendment of the Act on the Bank Guarantee Fund, p. 6.

10 As the explanatory note to the draft Act on the amendment of the Act on the Bank Guarantee Fund Law points out, the modification of Article 97 paragraph 7 involving the introduction of a 7-day time limit for giving opinions by the Polish Financial Supervision Authority, aims to improve and streamline the process of adopting and updating forced restructuring plans, p. 7.

to consult the Financial Stability Committee. The Committee's opinion covers the issue of the impact of the measures necessary to remedy the circumstances, which prevent or impede forced restructuring, on the level of systemic risk (ABGF, Art. 95/3). The opinion of the Financial Stability Committee, voluntarily requested for by the Bank Guarantee Fund, is therefore not binding. This opinion is not a binding ruling in the procedure for the application of the measures in question.

By applying the measures necessary to remedy the circumstances preventing or impeding forced restructuring, the Bank Guarantee Fund also issues recommendations for the bank (ABGF, Art. 95/1). The recommendations are to be issued in the form of an administrative decision taken as a resolution of the Management Board of the Fund. The recommendations may concern three categories of matters. The first category is the scope of activity of the bank. The second category of recommendations covers issues related to the capital structure of the bank. The third category of recommendations is made up of recommendations on matters related to organisation of the bank. Such recommendations may refer to changes in the organisational and legal structure to make it more simple or to separate particular businesses of the bank. The recommendations, pursuant to the provision of Article 95 paragraph 4 item 1 of ABGF, may also concern the provision of solutions to enable continuous and undisturbed operation of the bank, including in the event of forced restructuring. The subject of this category of recommendations is identical to some of the supervision measures falling within the responsibility of the Polish Financial Supervision Authority.

It is not possible to issue the recommendations without seeking an opinion of the Polish Financial Supervision Authority. As the recommendations are issued in the form of administrative decision, as in the case of the measures necessary to remedy circumstances that prevent or impede the conduct of forced restructuring, the norm expressed in Article 106 § 1 will be applicable. In view of the above, the Bank Guarantee Fund will only be able to issue the decision after the consultative body issues its statement. Therefore, a statement given by the consultative authority does not create a new legal relationship. An opinion on the recommendations, like the opinion on the application of the measures necessary for the remedy of circumstances which prevent

or impede the conduct of forced restructuring, has the character of a ruling. The content of the opinion, as already mentioned, is not binding on the body of forced restructuring. The opinion of the Polish Financial Supervision Authority is an element of the procedural material in a broad sense in the proceedings for the issue of recommendations for the bank and may influence the decision of the Bank Guarantee Fund in this matter.

However, the state of being not bound by a position of the consultative body or the obligation to act in cooperation may lead to significant practical problems (Biernat, 1979: 79). This is so, because mutually contradictory and exclusive, in terms of merits, decisions may be issued regarding a domestic bank: one decision issued by the Polish Financial Supervision Authority on the application of supervision measures, while second decision from the Bank Guarantee Fund on recommendations concerning the application of measures necessary to remedy circumstances which prevent or impede the conduct of forced restructuring.

5 Conclusion

The legal relationships between the authorities of the financial safety net as regards the planning of forced restructuring of banks are not of a coherent nature. These relations are mainly based on the obligation or the right to consult the Polish Financial Supervision Authority by the Bank Guarantee Fund. However, the model of cooperation between the financial safety net bodies is to a large extent illusory. The position of the consultative body is not legally binding on the Bank Guarantee Fund regardless of the legal basis for the cooperation. The cooperation of the bodies is merely of a formal nature. Therefore, the lack of strong enforcement of law becomes the problem regarding the currently applicable law. Setting time limits for the issuance of an opinion by the Financial Supervision Authority can streamline the process of planning forced restructuring only in terms of time frame. But this does not result in harmonisation of activities of those bodies in substantive terms. The normative solutions adopted may adversely affect the adoption and updating of the plans and, consequently, the process of forced restructuring. The standards governing cooperation between financial safety net bodies are therefore not effective in juridical terms.

Therefore, it should be proposed for the law as it should stand (*de lege ferenda*) to introduce mechanisms making the cooperation between financial safety net bodies more feasible. The functional links between the Bank Guarantee Fund and the Financial Supervision Authority could take the form of cooperation within a common team on forced restructuring and the issue of joint decisions.

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Financial Technology and Provision of Services – New Challenges in Consumer Protection in Financial Services

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Abstract

The present paper addresses the subject of financial services consumer protection in the context of the expanding use of new technologies in the financial services market. In contemporary times, the interface between the consumer of financial services and FinTech concerns a broad range of aspects, from the means by which the consumer acquires information about a service through determining the terms of the contract and its making, the innovativeness of products and services, to new business models. This gives rise to new potential risks and threats to the financial services consumer, and demands we initiate debate over the necessary scope of protection. The present work is a contribution to this discussion, and its objective is to present the risks that have already been identified as well as to indicate existing solutions and propose new ones in respect of both supervisory and legislative activities to mitigate the identified risks.

Keywords: Law; FinTech; Consumer Protection.

JEL Classification: D18; Q55.

1 Introduction

As the EU standard requires, the consumer on the single market is guaranteed a high level of protection, including the protection of safety and economic interests; and the EU, apart from those matters, is also to contribute

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to supporting the right to information[2]. This means *inter alia* that the consumer should be provided with conditions to make a free, independent and informed decision when choosing and purchasing goods and services. On the financial market, the key issues indicated within this scope are: ensuring the consumer obtains clear and accessible information facilitating a rational decision from among available offers (Jagielska, 2012: 252); and protection of economic interests during both the making of contracts in the seat of an institution and during the distance sale of financial services to consumers by e.g. excluding situations in which a consumer acquires a service that was not asked for ("inertia selling"), or the sale of services that are not relevant to the client's needs ("misseling"). The development of FinTech has a significant impact on the services provided to clients of the financial services market, and it creates new problems with respect to consumer protection. On the one hand, this impacts the broadly-understood innovativeness of services as provided (including creation and distribution); while on the other, it influences the expansion of their scope; new spheres of activity by enterprises based on new technologies naturally generate previously unknown challenges in consumer protection. In particular, this relates to potential threats to the realisation of three fundamental rights of the consumer: the right to reliable information, the right to safety, and the right to choice. Thus, from the perspective of the law, it is vital to determine to what extent FinTech impacts the behaviours of clients and financial institutions, and whether – and where – to consider legislative intervention in order to ensure appropriate consumer protection (introduction of new solutions, expansion of supervisory authorities' competences). With this in mind, the objective adopted for the present work is to define the potential risks and threats to the financial services consumer associated with FinTech, and to present existing and proposed solutions at the supervisory and legislative levels. The considerations are limited to indicating selected issues of financial services consumers with respect to the provision of services using financial technology, while avoiding certain issues

2 The notion of consumer protection and necessity of accounting for it in defining and realising other policies and activities of the Union was expressed in the Treaties themselves (generally in Art. 12 TFEU, specified in detail in Art. 169), and has thus found its expression in many legal acts of various ranks.

such as a broader discussion of risk of poor decisions by financial services suppliers in the event of mistakes in instruments of large databases, cybersecurity and data protection.

2 Standards of consumer protection on the financial market in the EU

In analysing the issue of consumer protection within the context of FinTech, it should first be pointed out that the development of technology will not solve existing problems. The pathologies and improprieties described in the literature still exist, but they are appearing in new guises. As regards information, the existence of the problem of information asymmetry on the financial market continues to be pointed out, and this must be linked with the potential for undesirable behaviours to occur: negative selection and the temptation to engage in abuses (Szpriner, 2009: 48; Oręziak, 1999: 19). In the behavioural sphere, in spite of progress made, we may still observe that a significant portion of society is unwilling to familiarise themselves with information, and there is a clear difference at the micro level between what consumers know about financial products and what they should, in fact, know (Lumpkin, 2010: 7). This is despite the fact that the legislator orders one party (the financial institution) to take responsibility for what the other party is supposed to know (Grzegorczyk, 2009: 130). Furthermore, mention should be made of individual possibilities of perceiving and understanding information that are the results of both educational attainment and personality traits; but of equal importance is the manner in which the information is presented. Not without meaning here is the fact that on many occasions, people operating within the financial sphere are without clear, stable, and ordered preferences (Orlicki, 2011: 201). In addition, the fact should be pointed out that, despite the accepted paradigm of the rational consumer seeking to maximise personal profit, in fact, consumers are frequently guided not only by sound judgment, but their decisions are also impacted by non-economic factors guided by emotional considerations (Nieborak, 2016: 46; Lefevre, Chapman, 2017: 6), heuristic selection methods, decision context., and the impact of the environment on preferences (Chrupczalski, 2008: 13). Thus, we may point to the presence of behavioural

effects on the financial services market. Consumers, in selecting a financial product or service, must deal with their own prejudices (e.g. term life insurance forces us to face the issue of our own death); they must process information about alternatives in order to come to a conclusion about the attractiveness of each alternative, while this choice is beset by mistakes that result from particular tendencies (such as a strong aversion to loss); and they may be disoriented as a product of the complexity or the sheer number of alternative solutions and associated high cognitive costs (Baker, Dellaert, 2018: 8)[3]. We must also not overlook the fact that it is difficult for consumers in such cases to learn from experience, as financial products are frequently one-off purchases (Lunne, 2014: 49).

Next, it should also be recalled that consumer protection has been and continues to be effected through ensuring the right to information and the right to choose. Regardless of whether a service is provided via FinTech or not, it remains true that institutions are obliged to provide the consumer with transparent and comprehensive information. Indeed, it remains a strategic assumption of contemporary consumer protection for the consumer to be supplied with information critical in making a conscious market decision, both in terms of the scope of the information presented and the manner of its presentation (Rutkowska-Tomaszewska, 2013: 327). In analysing the general standard introduced by EU regulations, it can be concluded that the financial market is subject to a model that assumes the provision of honest, transparent, and not misleading information. This concerns the insurance market[4],

3 With this in mind, when posing within the literature the question of the limits of legislative intervention taking into account the behavioural factor, indication is made of the natural question: should it be decided at the legislative/regulatory level what is in the best interests of consumers? To what extent, if at all, would such an approach respect consumers' freedom of choice and freedom to make mistakes? (Lefevre, Chapman, 2017: 27).

4 See among others: Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (recast) (IDD), OJ L 2016.26.19, in Poland: ustawa z 15 grudnia 2017 r. o dystrybucji ubezpieczeń, consolidated text: Dz.U.2018.2210, Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs), OJ L 2014.352.1.

banking[5], the payment market,[6] and securities[7]. In some areas, protection goes even further, where the enterprise is required to define the requirements and needs of the client, as well as to propose a contract aligned with those requirements and needs (Pokrzywniak, 2018: 71). Thus, the present standard is not only to facilitate consumers' assessment as to whether the proposed contracts are adapted to their needs, but also to their individual financial situation.

The issue of correctly informing consumers encompasses several spheres: scope of information, manner of presentation and transmission (access), and elimination of undesirable conduct is done here through statutory definition of information obligations and of the rules governing the provision of information to consumers. It is the legislator's objective to find solutions that require entities providing financial services to focus their efforts on composing messages within the framework of transmitted information for it to be formulated and communicated in a manner the consumer can understand and make use of, as opposed to performing the impose obligations merely, or primarily in order to limit legal risk. At the same time, the appropriate supervisory authorities are under an obligation to educate participants in the financial market, and to monitor tendencies and phenomena that may impact tasks associated with consumer protection. The objective of activities is also to develop common principles for disclosure of information. It should be emphasised that within the framework of such activities, there is research presently being conducted into the effectiveness

5 See Directive (EU) 2014/17 of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010, OJ L 2014.60.34, in Poland: ustawa z 23 marca 2017 r. o kredycie hipotecznym oraz o nadzorze nad pośrednikami kredytu hipotecznego i agentami, Dz.U.2017.819; Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers (CCD), OJ L 2008.133.66; in Poland: ustawa z 12 maja 2011 r. o kredycie konsumenckim, consolidated text: Dz.U.2018.993.

6 Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market (PSD2), OJ L 2015.337.35; Directive 2014/92/EU of the European Parliament and of the Council of 23 July 2014 on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features (PAD), OJ L 2014.257.214.

7 Directive (EU) 2014/65 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (recast), OJ L 2014.173 349.

of various methods of presenting information involving the participation of consumers, as well as studies focused on behavioural aspects of investment decisions taken by individual investors.[8]

3 Protection of financial services consumers in the context of existing risks associated with FinTech

Having in mind what we have discussed above, we can address the possibilities and benefits offered by the application of new technologies, as well as the identification of threats to the potential of consumers to invoke their rights. FinTech need not always create real dangers, and not all of them can presently be diagnosed, as it should be assumed that a portion of such threats is either difficult to predict or unpredictable. As for the issue of consumer protection in the context of FinTech, it can be examined from the systemic point of view (including the issue of the financial sector's resistance to cyber threats, the impact of digitisation on financial market competition, impacts on the business models of payment and credit institutions, electronic money, the effect of FinTech on restructuring credit institutions and investment firms, social financing based on the provision of loans), but also that of the individual consumer who comes into contact when purchasing a financial product, when engaging in activities related to a financial service, and taking advantage of additional services associated with a financial product and/or service. From the perspective of the market as a whole, as regards the issue of protection of the client, having in mind that in the collection, aggregation, storage, analysis, and use of data can involve multiple entities, questions arise as to whether participants have total control over their systems in the face of the growing dependency of financial institutions on: suppliers of technology services, "cloud" providers of computing services, infrastructure (e.g. servers), and software (e.g. applications). Do they ensure their clients' data is protected? Furthermore, what are the dangers and threats associated with faulty automation or the introduction of new business models? Thus, with regard to the range of benefits that come from FinTech

8 See Explanatory memorandum, Proposal for a Regulation of the European Parliament and of the Council on key information documents for investment products /* COM/2012/0352 final–2012/0169 (COD).

for consumers, it is necessary at the same time to define the potential risks that arise when introducing new products, services, and models, and in the selection of a particular service or product by the individual consumer. Indeed, it should be clearly emphasised that in many aspects FinTech has a positive impact on the manner in which services are provided, and by the same token on consumer satisfaction. For example, the automation of services is leading to a reduction in their costs, access to a greater number of products and services for a greater number of consumers is easier, and the quality of services rendered is improved based on e.g. the most current market data (Report on automation in financial advice, 2016: 8). The development of technology may eliminate customers' decisions being hobbled by behavioural defects. Studies demonstrate that automation may support consumers through the use of algorithms for solving complex optimisation problems (Baker, Dellaert, 2018: 8); FinTech application boost the availability of investments in retirement pensions for a broader group of consumers and increase the effectiveness of communication with savers (OECD, Technology and Pensions: 2017: 5); it becomes possible to develop unbiased recommendations that are a best fit to the needs of clients and to account for a broad range of cash flow strategies and scenarios. New technologies make it possible to transmit information to consumers encompassing a greater scope of consumer preferences in the manner of presentation, while consumers also have better insight into and control over their financial situation.

Analysing the fields of potential threats to the financial services consumer from the perspective of automation, it should be highlighted that, while there is no doubt it is present with varying degrees of intensity in various segments of the financial market[9], irrespective of the sector threats may develop at different moments in the relation between the provider of financial services and the consumer: when obtaining a recommendation concerning a product/service while establishing a relationship in an automated manner; when receiving information about an agreement; and in the performance

9 As studies show, the phenomenon of automated consulting is present in the banking, insurance, and securities sectors, but the scale and intensity differ across those sectors, and it would seem it is most present in securities (Report on automation in financial advice, 2016: 15).

and termination of the agreement[10]. Next, of significance for analysis of the scope of vital consumer protection is the fact that it may concern diverse aspects of the functioning of automated services. Firstly, account must be taken of mistakes in the functioning of the tool itself. These can result from mistakes when developing an algorithm (errors or biases in algorithms, errors in data constituting the basis of calculations), but also hacking and manipulation of an algorithm. This leads to the potential for injury to clients of entities providing financial services, and furthermore is linked with the potential for legal disputes to arise in the event of non-transparent assignment of responsibility (Report on automation in financial advice, 2016: 10). Secondly, in the case of automated advice, we should point to the frailty of automated tools in contact with clients. In particular, the potential emergence of misunderstandings by the consumer of information and the absence of the possibility for consumers to ask questions in order to get more precise information. Another issue may be that of conducting a technologically defined strategy of targeting a specified group of clients with services. This may lead to a failure to satisfy the needs of consumers with more distinct requirements, as nuances present in their needs may not be grasped by basic algorithms (FCA, 2017: 27). Full automation carries with it the threat of passing over the human element and the desire of consumers to have account taken of their own preferences (Fisch, Labouré, Turner, 2018: 14). Thus, an abuse of technology is possible leading to the absence of individualisation of consumers' needs, as well as other abuses like the introduction of a more profit-oriented robo-adviser that could take advantage of behavioural effects by pushing decisions taken by consumers in a direction that is in the interests of the consultant, rather than the consumer (Baker, Dellaert, 2018: 16). Another issue is the progressing refinement of algorithms leading them to become potentially inscrutable. This makes possible the emergence of the risk of so-called "black boxes" (ACPR's FinTech Innovation Unit, 2018: 9).

A separate issue that comes up in the context of FinTech is that of exclusion or limitation of access of particular groups of consumers to financial

10 It should be recalled that at present algorithms can be used by financial institutions in various ways, not only in setting prices or managing risk, but also in client relationships or in marketing.

products and services. This is present in many different aspects. Not only the ICT skills of particular individuals and the non-digital population being left behind, but also the exploitation of certain systems, algorithms, etc. by financial institutions. Several examples can be pointed out. The application of telematics and the use of wearable devices will facilitate the collection of richer data sets concerning consumer behaviour. This may, in turn, impact risk selection so that a certain group may find themselves priced out of financial services and products; for example, the absence of insurance offers owing to predictions of the client's potential health problems (EIOPA, Big Data, Retail Risk Indicators and Consumer Trends Report, 2017: 8; FCA, 2017: 27). Indication is made here of the general issue of the growing threat of exclusion of vulnerable consumers through the automation of services (this can concern different groups of people, such as those with a criminal record, with poor credit history, but also untypical clients such as individuals with a defined type of disability). The extent of this danger grows in the event a large number of suppliers take advantage of the same system for service automation (FCA, 2017: 27). Similar threats, albeit from a different perspective, are also indicated by supervisory authorities which emphasise that the potential growing extent of client segmentation, made possible owing to large collections of data, is giving rise to unwanted effects within the scope of access to and accessibility of some financial products and services (Report on the Impact of FinTech on Institutions' Business Models, 2018: 23).

Another issue that needs to be taken into consideration is the use of new technologies in the transmission of information to consumers. It is possible to employ instruments that distract attention from important information, or make it difficult to receive; we may point to present regulations prohibiting such practices, such as when information is supplied using techniques such as terracing of windows and pop-ups[11]. On the other hand,

11 For example, pursuant to Art. 18 of the Commission Implementing Regulation (EU) 2018/33 of 28 September 2017 laying down implementing technical standards with regard to the standardised presentation format of the statement of fees and its common symbol according to Directive 2014/92/EU of the European Parliament and of the Council (OJ L 2018.6.26), electronic instruments cannot be obtrusive, so as not to distract the consumer's attention from the information contained in the transmitted materials.

the selection by the consumer of a digital device (e.g., a mobile telephone) to achieve access to a product or service may lead to insufficient caution on the part of the consumer, or failure to pay sufficient attention to the terms and conditions of the offered service or product (FCA, 2017: 27). It would seem that this is a particular threat to the younger generation of consumers, which results from their behavioural-based preferences (so-called "visual culture" – visual messages communicate more to them than text, aversion to long consultation processes, etc.).

It should be mentioned in closing that the digitalisation of finances leads to the appearance of new products and services outside the traditional financial sector, such as P2PL electronic platforms that create numerous threats to consumers, both lenders and borrowers (Rogoń, 2017: 43–44). The literature indicates *inter alia* the potential for the consumer to lose the sum loaned (Macchiavello, 2017: 662) or the failure of the consumer to recognise the risk that results from reliance on misleading advertisements or unverified information, particularly about the consumer borrower and that borrower's project (Cherednychenko, Meindertsma, 2018: 5).

The diagnosed and indicated risks associated with FinTech on the financial market justify giving consideration to the necessity of changes to the law and the introduction of solutions accounting for new threats to consumers on the financial services market. This is all the more true that, as the European Parliament has emphasized, "*the same consumer protection standards apply to FinTech services as to other financial services, irrespective of the channel of distribution or the location of the customer*" (European Parliament resolution, Recital 45). It should, however, be observed that, in seeking to protect the consumer with consideration to the complexity and diversity of new issues arising, it is not advised to seek out one perfect solution, but rather direct action within the spheres of identified risks. However, as previously, any potential new duties of entities providing services on the financial market must concern services and products being introduced, as well as monitoring of the manner of service delivery based on modern technologies.

For protection of the consumer on the financial services market, the adopted standard is one of testing a product before it is brought to market[12]. When it comes to FinTech, supervisory bodies seek joint participation in the process of testing through a sort of cooperation of such bodies with the entities that supply financial services, as well as in the creation of conditions for the controlled application of new solutions based on technology. Presently, two solutions in particular are promoted: regulatory sandboxes and innovation centres. Sandboxes allow for testing of innovations in a safe environment, most frequently with substantive support from supervisory bodies giving the possibility developing new, safe services (on the other hand, they give supervisory authorities the opportunity to look over financial innovations from the perspective of potential threats to consumers as early as the testing phase). The final impact of testing innovative financial solutions within the framework of sandboxes on ensuring consumer protection will only be suitable for assessment from the historical perspective, although it seems at present an optimal solution. Here it should also be mentioned that in perceiving the benefits of the existence of a controlled space in which an innovative service or product can be tested, solutions protecting consumers are introduced as the testing phase involves the participation of real clients. Protection can also be achieved through exclusion of the possibility to engage client funds, or a system of guarantees for participants. A separate issue is that of the principle of information and consent to participation in a regulatory sandbox[13]. However, information centres allow enterprises to obtain (usually non-binding) answers to questions concerning *inter alia* the applicability of consumer protection regulation (Report FinTech: Regulatory sandboxes and innovation hubs, 2019: 14). This allows

12 Pursuant to EBA guidelines, before a product is brought to market, it should be tested in a manner that facilitates assessment of its impact on consumers, including in extreme conditions. Guidelines on product oversight and governance arrangements for retail banking products, EBA/GL/2015/18, 22/03/2016 https://eba.europa.eu/documents/10180/1141044/EBA-GL-2015-18+Guidelines+on+product+oversight+and+governance.pdf

13 Essentially, the functioning within the EU of regulatory sandboxes is not regulated at the statutory level; however, in some states, such as Spain, statutory solutions are currently being prepared (see draft "Ley de medidas para la transformación digital del sistema financiero" of 11 July 2018).

enterprises to be better prepared to perform their duties in respect of consumer protection.

As concerns monitoring the manner of provision of services based on or with the use of modern technologies, the subject literature contains proposals of various solutions. For example, protection could be ensured for consumers through the introduction of a system registering automatic advice, which would facilitate assessment of the service based on records, as well as the causes of systematic discrepancies between advice and actions taken (Baker, Dellaert, 2018: 18). Another proposed solution is the development by supervisory authorities of a list of requirements for automated consulting systems and so-called input/output tests. These tests, based on standardised scripts, would facilitate examination of tools from various suppliers in terms of compliance with the authority's recommendations (Baker, Dellaert, 2018: 23).

Another issue within the scope of consumer protection is that of implementation of the right to information within the context of appropriate understanding of the characteristics of a product or service, and of the risk associated with it. Presently, regulations are concentrated on the manner of presentation of information[14] and its scope. This concerns both information transmitted in the traditional manner as well as with the use of electronic means. Unresolved remains the issue of preparation of the consumer to undertake the effort of reviewing the properties of a give financial product or service. At present, legal regulations place on supervisory organs at the European and national levels distinct educational duties, which are to be a response to the problem of insufficient knowledge and awareness of the consumer of financial services.

14 In some cases, regulations are very detailed, covering font sizes, order of information, headers and subheaders. As has been mentioned, there is also a prohibition on distracting the recipient of information, e.g. the application of electronic means may not distract the consumer's attention from the information.

Pursuant to the EBA Founding Regulation[15], EIOPA Founding Regulation[16], and ESMA Founding Regulation[17] the tasks of European Supervisory Authorities include "reviewing and coordinating financial literacy and education initiatives by the competent authorities" (EBA Founding Regulation, EIOPA Founding Regulation, ESMA Founding Regulation, Art. 9(1)(b)). Detailed tasks of the authorities of particular states within this scope are determined by national legislation.

As studies demonstrate, the relevant authorities in individual EU states engage in a range of educational initiatives, employing various sources and means of contact (including leaflets and guides, website and online tools, social media, phone/email, competitions, media, consumer helplines, seminars, and conferences), targeting all consumers or specific groups, such as school-age children (EBA Financial Education Report: 12). Most frequently, the transmitted knowledge concerns a specific issue concerning knowledge of the financial market, in accordance with a need for the education of consumers diagnosed by those authorities in a given area (for example, emerging market trends); some of the initiatives undertaken are associated with the struggle with financial exclusion (EBA Financial Education Report: 12). In some states, there is a Consumer Hub which provides continuous, comprehensive and accessible knowledge on the financial market, including FinTech[18]. Nevertheless, none of the indicated initiatives eliminate certain behavioural conditions of financial services consumers, such as the previously indicated insufficient attention paid to the offer of services by telephone. Thus, consideration may be given to whether it is justified to enact broader protection

15 Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC, OJ L 2010.331.12.

16 Regulation (EU) No 1095/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Securities and Markets Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/77/EC,OJ L 2010.331.84.

17 Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC, OJ L 2010.331.48.

18 Such an initiative was undertaken by the central bank of Ireland (https://centralbank.ie/consumer-hub).

through the imposition of additional duties on the provider of a financial service (for example, in cases of automatic recommendations, verification of the extent of understanding of the character of the product/service prior to the final conclusion of the contract, and in the event of negative assessment the necessity of making contact with personnel from the financial institution), or the introduction of new competences for supervisory authorities in the form of confirmation of standard-form contracts prior to the introduction of a product or service onto the market.

In completing this portion of the considerations, we may also signal that in respect of social financing, consumer protection can be ensured at the statutory level by introducing separate regulations (for example, Spain has adopted an act regulating the operation of platforms[19] that protects non-professional investors); however, in essentially the majority of states and at the EU level, existing provisions are cited[20], and legislative work in the EU is presently aimed only at support for cross-border financing of economic activity through regulation of social financial services[21]. It should be pointed out, however, that such protection is not always effective (Rogoń, 2017: 43–44).

4 Conclusion

Ensuring a high level of protection for consumers of financial services in the context of FinTech would require the lawmaker and supervisory authorities to examine potential threats taking into account two fundamental factors:

- technological risk;
- behavioural predispositions of consumers.

19 Ley 5/15, de 27 de abril, de fomento de la financiacion empresarial, BOE núm. 101, de 28 de abril de 2015, p. 36599.

20 For example, it is considered that "when a consumer is receiving a loan for personal consumption and operating outside of professional capacity this activity falls within the remit of the Consumer Credit Directive", see: Proposal for a Regulation of the European Parliament and of the Council on European Crowdfunding Service Providers (ECSP) for Business COM/2018/0113 final–2018/048 (COD). Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52018PC0113

21 Proposal for a Regulation of the European Parliament and of the Council on European Crowdfunding Service Providers (ECSP) for Business COM/2018/0113 final–2018/048 (COD). Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52018PC0113

In respect of the former, this concerns the development of solutions enabling consumer protection when a tool functions improperly. In particular, firstly, preventing the introduction onto the financial market of services in which processes or sets of rules applied in operations may contain either deliberate or unintentional mistakes. This means transgressions resulting from susceptibility to threats from the construction of the algorithm, such as mistaken assumptions, biased logic, cognitive biases of the creators of models, unethical criteria (risk associated with the "ethics" of algorithms), and changes themselves to the character of algorithms (the tendency to replace programmed algorithms with "self-learning" algorithms), increasing the risk of "black boxes." The exclusion of services or products containing errors in algorithms entails the necessity of testing and checking an algorithm before a service or product can be made available to consumers. This has led to the current introduction of regulatory sandboxes allowing the testing of an innovative financial service, and allowing supervisory authorities to assess it from the perspective of *inter alia* consumer protection. Secondly, errors in the functioning of a tool can result from the hacking or manipulation of an algorithm (they can arise despite the implementation of appropriate security systems). In this regard, it is necessary to define a clear assignment of liability and to ensure for the consumer the possibility of simplified pursuit of claims in the event injury arises.

In respect of the latter, this concerns in particular the introduction of solutions to limit the negative impacts of some conduct potentially constituting a threat to both individual consumers and groups of them. Naturally, in every case it is necessary to first determine the scope within which to intervene in response to the question of the extent to which a client is free to make mistakes. There are many important factors to take into account here, as well as values protected on the market and determination of the consequences for e.g. stability of the financial market. In this paper particular attention has been paid to the problem captured by the question of how the legislator should proceed with respect to the various forms of aversion to familiarising oneself with information about a financial service? In respect of automation of advice, one solution could be obligatory linking of automated advice with personal contact (Bionic Advisor) at the present level of technological

development, or confirmation of standard-form contracts by a supervisory authority in respect of services offered via telephone. It would seem that these solutions can help eliminate some of the risks, but they remain linked with the broader issue of increasing the level of awareness on the part of consumers as regards the consequences of their decisions and responsibility for taking them.

In summarising the considerations presented in this paper, it can be pointed out that insofar as the threats resulting from new technologies and their application on the financial market are increasingly recognised, solutions preventing particular risks are not infrequently at the stage of testing, while in other cases remedies are still being sought.

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FINANCIAL LAW
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Financial and Legal Aspects of the Organisation of the Labor Protection in Russia

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Abstract

This contribution deals with the main issues of financial provision of labor protection measures in accordance with Russian legislation, and also a number of the provisions of the draft law on the introduction of amendments and additions to the Labor Code of the Russian Federation for the ensuring the healthy and safe working conditions by the employer at workplaces. The main aim of the contribution is to confirm the aspiration of the state to interest employers economically to improve working conditions at workplaces. It depends on: varying the amount of insurance premiums, reducing the price of the procedure of special assessment of working conditions as instrument of definition of existence of harmful and dangerous production factors, establishing the obligatory list of the actions for labor protection financed by employers. From the legal point of view the special attention is paid to the planned radical changes of the legislation on labour protection. There are regarding changes of conditions of the employment contract, formulation of the major principles of providing healthy and safe working conditions, need for employers to define and practically to realize the policy in the field of labour protection according to the main directions of state regulation.

Keywords: Labor Protection Financing; Labor Legislation; Healthy and Safe Working Conditions; Employer's Obligation; Employment Contract; Social Insurance; Accident.

JEL Classification: I10.

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1 Introduction

The Constitution of the Russian Federation adopted on 12 December 1993 guarantees to each worker the right to work in the conditions meeting safety and hygiene requirements. Article 210 of the Labor code, the major regulatory legal act, governing the labor relations in the country, designates the main directions of state policy in the field of labor protection and first of all it points to providing a priority of preserving of the life and health of employees. Recognizing the need for observation by epy employers of the basic rules which are characteristic of the modern market economy, the state must be nevertheless essentially in the aspiration to provide such working conditions which are conform to the international standards for hired workers. By historical standards the state passed to the market principles of creation of economy rather recently whereby the influence of many provisions of the Soviet labor law can be considered positive on the modern legislator.

The Russian labor protection legislation is multilevel now. It is rather detailed and is potentially capable to provide successfully protection of the workers from harmful and dangerous production factors in the workplace. At the same time, there are some problems of economic and legal character interfering normal realization of these regulations. The most critical of these problems are the following:

- quite low social orientation of many Russian employers who first of all are focused on the receiving of profit, but not on the social partnership;
- insufficient efficiency of the state supervision of observance of labor rights of workers;
- the gaps of the legal equipment reducing the potential of a number of precepts of law on labor protection.

At the same time, activities of the state for correction of current situation allow to look forward at the bright side of the things.

2 The financial side of the issue

Article 226 of the Labor Code of the Russian Federation defines that the financing of actions for improvement of conditions and labor protection is mandatory at the expense of budgets of all levels from the federal to municipal budgets. Also there is the attraction of non-budgetary sources of financing and the most typical source there is the means of the employer ("Collection of the legislation of the Russian Federation", 7. 1. 2002, N 1 (p. 1), art. 3).

The referenced article orders to the employers to allocate, at least, for these purposes 0,2 % of a cost amount for production, performance of works or rendering services. The structure of such costs is already defined by the legislator, it is the order of the Ministry of Health and Social Development of the Russian Federation dated 1 March 2012 No. 181n that established the standard list of annual actions for the employer to improve the conditions and labor protection and to reduce professional risk levels. This list is rather extensive and includes a significant amount of actions. In terms of their potential the most important of them can be the following:

- evaluation of the working conditions (till 1 January 2014 there was the assessment of workplaces under the terms of work) this allows to define the production factors, if they are in a workplace that can be dangerous or harmful and to estimate their level of impact on the worker;
- providing the separate employee categories with means of individual and collective protection;
- organization of the training and examination of workers for safety knowledge assessment;
- performing obligatory medical examinations, there are preliminary and periodic surveys.

Except such basic actions, a list contains also lower points but also rather significant, for example, application the alarm colors and signs of security on production equipment; acquiring and installation of drinking water cooler for those workers who work on productions with high temperature of air indoors; organization of epy training of workers in acceptances of first-aid treatment to victims at the production, etc. (Bikmetov, Kirsanov, Tishin, 2015).

A number of the Russian jurists have some objections in the wording of Article 226 of the Labor code. So, A. Petrov notes that on branch accessory a number of its provisions belongs to the financial law therefore they can be quite withdrawn, and the article can be supplemented with the instruction that the employer has the right to create the fund of the security and occupational health, at the same time the worker does not incur any financing expenses of actions for labor protection (Petrov, 2018: 17–21).

At the same time the state tries to stimulate the fair employers seeking for providing healthy and safe working conditions. For example, in Article 7 of the Federal law "About Special Assessment of Working Conditions" it is specified that results of special assessment of working conditions can be used when calculating discounts to an insurance rate for compulsory social insurance from occupational accidents and occupational diseases and also for justification of financing of actions for improvement of conditions and labor protection, including at the expense of funds for the corresponding insurance ("Collection of the legislation of the Russian Federation", 30. 12. 2013, N 52 (part I), art. 6991).

In general, the specified regulations are introduced as progressive and capable to stimulate the Russian employers to improve working conditions in workplaces. At the same time, a specific of relationship of workers and employers in the conditions of the Russian market economy is so that employers, in the absence of proper state supervision often try to save on ensuring labor protection of workers. It is a case in point that is explained by such aspiration to the rather widespread practice of the employment of workers without execution of the employment contract. At first sight, it is rather favorable to the employer, officially he should not incur expenses on the providing healthy and safe working conditions. Besides, there is an economy not only on the tax assignments but also on a number of guarantees which are established by the labor law (Kochanova, 2019: 95–110). It is obvious that similar situations can appear in large quantities when the state is not able to supervise effectively for the observance the rules which are established by the state.

The situation with supervision is often far from optimistic. The main supervisory authority in this sphere is a State Labour Inspection in territorial

subjects of the Russian Federation, in the republics, regions, areas, the federal cities, the autonomous region and autonomous areas. Unfortunately, the number of staff of inspections of work in areas is exposed to reduce in the last decade for the purpose of budgetary funds economy.

For example, such researcher as A. V. Mikhaylov points to the fact that at the system of checks accepted now State Labour Inspection only in the organizations of the Moscow region it can take not less than 28 years (Mikhaylov, 2011: 65–71). According to the data provided by A. A. Shugayev, the quantity of unaccounted occupational accidents in Russia only in 2011 was about 2,5 million (Shugayev, 2015: 173–182). The way out this difficult situation seems only one: the state has to draw a close attention to a condition of State Labour Inspection in areas and increase the number of inspectors. Costs from the budget for their contents, certainly, will pay off due to decrease in level of occupational injuries.

Besides, it is necessary to mention also the aspiration of the state to achieve the improvement of a situation in the field of labor protection with a bit different way and it is the stimulation of the employers, that can let them know that it is possible to achieve significant economy of means with the providing of the normal working conditions. G. S. Skachkova notes that it is required the further improvement of the system of obligatory insurance of professional risks, proceeding with the individualization of the process from the perspective of types of the activity of employers. Certain steps are taken in the recent years. For example, with the adoption of the Federal law "About Special Assessment of Working Conditions" since the 1 January 2014 the tariffs of additional insurance premiums in the Pension Fund of the Russian Federation and some other funds are established with the consideration of the division of the working conditions in the degree of harm and in classes and subclasses (Skachkova, 2014: 13–14). There are four classes of working conditions mentioned in the Federal law, proceeding from the level of harmful and (or) dangerous factors in the workplaces: optimum (the 1st class), admissible (the 2nd class), harmful (the 3rd class with four subclasses depending on the harm level), dangerous (the 4th class).

3 Some legal aspects of labour protection

As it was already noted above, the Russian legislation on labor protection is rather harmonious. At the same time, as of today, there is available many provisions needing adjustment.

The Ministry of Labour and Social Protection of the Russian Federation prepared the federal law draft in 2016 about the introduction of amendments to the Labor code regarding the improvement of mechanisms of injury prevention and professional incidence, observance of the labor law and other regulatory legal acts containing regulations of the labor law (http://base.garant.ru/56736395/#friends).

Among the key moments of this draft that already passed the anti-corruption examination it is possible to allocate the following.

The Labor code will include the Article 209.1 and there are the basic principles of the safety of the workers in the article. It is difficult to overestimate the importance of the emergence of this article because it is referring to the basic, fundamental provisions defining the key components of the labor protection. One of such components is the declaration of the priority of prevention of occupational injuries and professional incidence. The Russian system of labor protection, as well as its analogs in other countries, proceeds on the basis in recent years that it is easier to prevent an accident at the workplace, than later to eliminate much more substantial negative effects.

Also the principle of professional risks assessment is very important in this connection. It is connected with the previous logically and closely.

The employer, at last, will be given the right to discharge of work of the worker who is not applying the individual protection equipment issued to him in accordance with the established procedure. In the current Article 76 of the Labor code the employer has no similar potential. Certainly, the worker who is not using as appropriate individual protection equipment can be brought in accordance with the established procedure to disciplinary responsibility; however, it cannot solve the current problem, and does not give to the employer the chance to react quickly to the mistake

made by the worker. At the same time the legislator gave the chance of fast and effective permission of the designated problem.

By the federal law from 30. 11. 2011 into Section XII "Features of the regulation of work of separate employee categories" of the Labor code the new Chapter 51.1 was entered it is "Features of Regulation of Work of the Workers Occupied at Underground Works". After the investigation of the tragedy in the Raspadskaya mine in 2010 when 91 persons died, measures for improvement of legal regulation of work of underground workers were arranged first of all, from the positions of providing healthy and safe working conditions.

So, there are five articles entering Chapter 51.1 and four treat labor protection. Article 330.4 is of special interest, in according to which the employer is given the right of discharge of the worker from work if he does not observe the established safety requirements at accomplishment of underground works and also does not apply the individual protection equipment issued in accordance with the established procedure. The bill provides to the employer of an opportunity to discharge on this basis all workers, and not just occupied at underground works. Such offer is submitted very correct and timely.

It is supposed to include the employer's obligation for the management of professional risks taking into account specifics of the activity into the article devoted to his obligations in the field of the labor protection that will promote to increase the employer's attention to the questions of the safe organization of the production. There is the actually obligation taking into account a modern situation to stop temporarily (before threat elimination) the activity of the production sites and also the operation of units, objects, buildings or constructions, the implementation of separate types of the activity at the emergence of the threat of life and health of the workers.

It is still going the state policy aimed at the right of the worker to the information in the field of the labor protection. In the bill there is the consistently developing idea that the worker has to receive all necessary information about the characterizing of the working conditions and the corresponding guarantees provided to him by the employer. After the state passed from the assessment of work places under the terms of work to more formalized

and tough procedure of special assessment, the requirements to the employers in this direction became also more rigid.

In particular, already at the stage of the conclusion of employment agreement the worker has to be informed about the harmful or dangerous production factors at his workplace and also what measures will be undertaken by the employer for his protection. It concerns so-called "the protection time" (establishments of additional breaks, reduction of operating time in harmful and dangerous conditions, granting the additional paid holidays), providing with special treatment-and-prophylactic food, granting means of individual and collective protection.

If the workplace is liquidated because requirements of labor protection were violated, the employer will be obliged according to the bill at the expense of the means to provide the worker with the additional professional education.

Also the bill offers refining of the formulation of the basis of dismissal of the worker at the initiative of the employer according to the subparagraph "d" point 6 of the first part of Article 81 of the Labor code. Now on this basis the employer can dismiss the worker for violation of requirements of labor protection if it caused heavy consequences (accident, trouble, an occupational accident) or obviously created real threat of approach of such consequences. But similar violation must be previously established by the labor protection commission or representatives for labor protection.

But the problem is that the specified bodies should not be created without fail in according to the Russian labor law and can treat bodies of social partnership. If they are absent the employer is actually deprived of an opportunity to stop labor relations with the worker on this basis. The draft enters into number of the bodies establishing the fact of violation of requirements of labor protection, the commission on accident investigation and such commission has to be created without delay by the employer in cases when there is an accident with the production worker. Such innovation can promote more effective legal regulation of labor relations.

Following the results of the investigation of the accident which happened on production to the worker the commission is obliged to draw

up the statement of H-1 form where it has to point along with circumstances of accident the perpetrators and the relevant standards of the labor law. This information will be the basis for the dismissal of the worker who allowed the violation.

In the near future it is offered to oblige the employer to develop and realize the policy in the field of the labor protection. It will have the form of the declaration like the local statutory act and define the main activities and obligations of the employer for ensuring labor protection of workers with the indication of means and ways of providing such obligations. Perhaps, for the first time in the Labor code there will be the instruction on the need for the employer to form corporate culture of labor protection and to propagandize a healthy lifestyle and also to seek for decrease in the financial expenses and losses connected with health damage of the worker who executes the labor duties.

At last, it is the important thing to include into the draft in the text of the Labor code in Article 226 according to which the employer will be obliged to consider not only the serious injuries of health received by the worker during a working activity but also microinjuries (microdamage) there are grazes, bruises, bruises of soft fabrics, etc. Getting similar microinjures by workers in many cases is connected with the wrong organization of working protection by employers therefore their accounting will potentially promote the prevention of obtaining health by workers of more significant injures.

It is possible to criticize a well-known Pyramid of Heinrich, but, according to the author of the present article, it is quite obvious the connection and influence microinjuries with a possibility of the approach of heavy accidents with workers. The author, preparing materials for the thesis, performed duties the public inspector of work in the state inspectorate about a year. That received experience and that statistics of incidents with workers confirm that there cannot be fine and insignificant details in questions of the labor protection. The neglect of employers to the safety issues increases inevitably the negative impact on workers. The obligation not only to consider, but also to analyze the reasons of microinjuries will force employers to pay closer attention to the safety issues on production.

4 Conclusion

Consequently the Russian legislator seeks for improvement of the available provisions now. These tasks can be considered both simple and rather difficult at the same time there is the task to conciliate the interests of labor and the capital and to make so that the worker will be rather effectively protected according to the labor protection positions. These mutually exclusive trends are caused by specifics of the development of the Russian labor law. On the one hand, it tries to meet the requirements of the modern market economy that treats rather calmly social inquiries of workers. On the other hand, there are still many provisions of the former Soviet labor law in it. Many workers, especially preretirement age, remember these provisions rather well, they expect the state paternalism and thereof are especially vulnerable to unfair employers.

The measures, that are taken now, can be considered rather effective, but the question consists in the possibility of the state on behalf of the supervisory authorities to provide effective observation of observance of the key moments of providing healthy and safe working conditions. Without radical change of the state approach to the status of supervisory authorities it is hardly possible to expect success. It is one hope only that common sense will prevail and will win over reasons of illusive economy of means of the government budget. It is still important to solve optimal tax connected with labour. According to Allcott et al. (2019: 1557), the optimal sin tax is increasing in the price elasticity of demand, increasing in the degree to which lower-income consumers are more biased or more elastic to the tax, decreasing in the extent to which consumption is concentrated among the poor, and decreasing in income effects, because income effects imply that commodity taxes create labor supply distortions.

Key points of the economic policy of the state concerning employers can be considered the following:

- obligation of the employers to ensure performance of the standard list of measures for providing healthy and safe working conditions and budgeting for these purposes in the set limits;

- further improvement of arrangements for special assessment of the working conditions including the reduction of expenses of the employer for the implementation in comparison with earlier applied assessment of work places;
- supporting the State Labour Inspection in regions for an opportunity to supervise effective for the compliance with the requirements by employers under the labor law, first of all it is the safety and health protection. For this purpose it will be required to improve their financial and staff assistance, to provide their additional legal protection.

Looking at the improvement of legal norms (however, such improvement is very closely connected also with economic problems) it is required first of all the following:

- accretion of power of the employer on the dismissal from work the workers who are not using the given them equipment for individual protection (glasses, respirators, gloves, etc.) which is properly;
- specification of the formulation of the dismissal of the worker who violated requirements of safety and health protection and the inclusion of the Commission on accident investigation as the subject establishing such fact will improve efficiency of the legal norms;
- at last, ascertaining of the obligation of employer to consider documentary not only essential accident threaten life and health of the worker, but also so-called microinjuries.

Apparently, all written above directions do not demand huge efforts from the state represented by its bodies, but they are capable to change considerably a situation in the field of the safety and health protection.

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Concept of Beneficial Owner of Income. Approaches of Russian Legal Proceedings

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Abstract

Tax optimization concerns important taxpayer rights, which is also a response to government tax incentives in certain branches. Nonetheless, tax minimization spreads into three big components, from a completely legal tax planning, to tax evasion, and between the two lies an area of increased risk for all participants in legal tax relations, which is now defined as tax avoidance. By conducting this research, a clear objective stands in front of us; that of confirming the hypothesis that in our current time tax authorities of Russian Federation only begin to get acquainted with the term "a beneficial ownership".

Keywords: Tax; Law; International Taxation; Beneficial Owner; Beneficial Ownership; Tax Treaty; Automatic Exchange Of Information; BEPS; MLI.

JEL Classification: K33; K34.

1 Introduction

No one likes to pay taxes. Some dislike it more than others. Most of us pay taxes because we recognize that to get what we want from government, we need to help pay for it. There is a kind of moral or social responsibility to pay our taxes – even if it hurts. But of course not everyone feels this way. Many will do whatever they can to avoid taxes even though this means that others will have to pay more just to make up what they have avoided (Steinmo, 2018).

Throughout activities of taxpayers are rarely guided by the interests of the government, yet paying taxes is not a right, but it is in fact an obligation for

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which compliance there will be no personal reward, only a public benefit. The conjunction of the requirements and obligations to pay taxes represents an important condition for the existence of tax systems among governments. We can use a rather colorful description of the entire process of tax minimization overtaking the spirit of tax law, as proposed by Krzysztof R. Woźniak: the taxpayers are located in a cyclops' cave, and we can easily suspect that there is always someone to deceive them. In order to break free (here: to take the tax burden out of himself), the taxpayer – Ulysses – prepares to fight with the settled order and – under the ram's stomach – gets out of the area under the cyclops control taking advantage of the cyclops'-state's blindness; blindness inflicted while the cyclops was not awake (Woźniak, 2018: 91).

The problem is that being large consolidated taxpayers, corporations have a lot of possibilities to avoid taxation, to leave their national tax domiciles due to offshore schemes and to choose the minimal tax rates domiciles, tax havens. In this sense compared to an average taxpayer the efficiency of their taxation has decreased dramatically (Chernikova, Gorosh, 2017: 284).

Most countries levy withholding taxes on outgoing dividends and interest payments to foreign affiliates. Tax treaties reduce or eliminate these withholding taxes on a bilateral basis, thus providing an advantage to foreign investors from the partner country. When multinationals engage in treaty shopping, they may obtain benefits that a host country would otherwise not provide to them (Weyzig, 2012).

The term "treaty shopping" has never featured in any versions of the OECD Model. Nor has it been properly defined or explained in the OECD Commentary. Rather, the emphasis is always on eliminating treaty shopping and the measures that can be taken against it. Most of the references to treaty shopping are references by default; i.e. when discussing anti-treaty shopping provisions (Avi-Yonah, Reuven, 2010).

But, according to the OECD Glossary of Tax Terms, "treaty shopping" refers to "*an analysis of tax treaty provisions to structure an international transaction or operation so as to take advantage of a particular tax treaty. The term is normally applied to a situation where a person not resident in either of the treaty countries establishes an entity in one of the treaty countries to obtain treaty benefits*." (OECD)

The OECD added the beneficial ownership clause to its Model Convention in 1997 to prevent tax abuse through treaty shopping (Vern, 2009: 138).

According to the OECD Glossary of Tax Terms "beneficial owner" is "*a person who enjoys the real benefits of ownership, even though the title to the property is in another name. Often important in tax treaties, as a resident of a tax treaty partner may be denied the benefits of certain reduced withholding tax rates if the beneficial owner of the dividends etc is resident of a third country*" (OECD).

The concept of a beneficial ownership refers to anti-avoidance rules, however it is a relatively young legal institution, although the authors state that the first use of this term can be traced back to 1942 (Demin, Nicolaev, 2018). Nonetheless, to this day there is no unequivocal understanding and interpretation. To a greater extent, this happened due to the fact that there is no unambiguous and generally accepted definition of the term itself. As a result, to this date its definition does not exist at OECD level; therefore, in most cases, its application must be limited only to a general understanding and to judicial discretion.

At the same time, it can be noted that there are great prospects for the development of this concept.

From a tax perspective, knowing the identity of the natural entity behind a jurisdiction's legal entities and arrangements not only helps that jurisdiction preserve the integrity of its own tax system, but also gives treaty partners a means of better achieving their own tax goals.

Transparency of ownership of legal entities and arrangements is also important in fighting other financial crimes, such as corruption money laundering, and terrorist financing, so that the real owners cannot disguise their activities and hide their assets and the financial trail from law enforcement authorities using layers of legal structures spanning multiple jurisdictions.(IDB and OECD, 2019: 2).

Prior to the introduction of the legal definition of "a entity with a beneficial ownership of income" in the Russian Tax Code, the term was mentioned in international agreements on the avoidance of double taxation, which were ratified by the Russian Federation and allowed the tax authorities to use it and to concretize it in their instructions.

Based on these documents, it is possible to trace the evolution of this term in Russia.

2 Formal periodization of the development of the term in the proceeding of Russian Federation

The term "person with a beneficial ownership of income" appears in agreements on avoidance of double taxation, which were signed at the time by the USSR, but for a long time this term was not used in its meaning. A certain evolution of approaches to its use and interpretation is traced in the instructions of the tax authorities. So, in the instruction in 1992, this term was not being paid attention at all. In the instructions of 1995 more importance was attached to the formal side of the issue, since it was assumed that the right to income could represent a condition for tax refund, however this right of the foreign organization was automatically confirmed in the moment in which a corresponding return statement was signed, and no further control was exercised. After the appearance of the Tax Code of Russia, the instruction to Chapter 25 also appeared, which regulated the tax in correlation to the income of the organization. It gave a more detailed interpretation of the term, however, as the authors rightfully note, this interpretation raised many questions, since it assumed a universal distribution of this term regardless of whether such reference was made in accordance to the corresponding agreement. However, the term was used to represent the existence of legal grounds for gaining income rather than being used in the same way as we do now and in the way that it was used by other OECD countries (Bruk, 2013: 54–62).

Subsequently, the "tune-up" of this concept already took place using explanatory letters from tax and financial authorities, which are also based on the explanations to the OECD Model Tax Convention on Income and on Capital.

In 2014 Art. 7 of the Tax Code presented some changes, as a result of which the beneficial owner of income was defined for the purposes of the code and of the international agreements on the avoidance of double taxation.

According to this definition, a beneficial income owner is defined as: an entity (foreign structure without a legal entity) who, due to direct and/or indirect participation in an organization, to the control over an organization (foreign structure without a legal entity) or due to other circumstances, has the right to independently use and/or dispose of the income received by such organization (foreign structure without a legal entity).

In their explanations, the tax authorities now indicate that a person with a factual right to income is a universal tool in fighting the abuse of tax agreement rules. On the other hand agreements regarding double taxation cannot be applied to situations where the relationship behind the provision of financing and the payment of income is not related to the attraction of foreign capital into the Russian economy, and the actions of the participants of such relations are only aimed at creating a convenient (concessional) tax regime. Benefits under international agreements on the avoidance of double taxation apply only to a tax resident who represents the beneficial ownership of income (Arakelov, 2017: 45–56).

After all of these changes begins the active stage of the formation of judicial proceeding in these categories of cases.

Nevertheless, the concept of an entity with a factual right to income is often used in court along with the judicial doctrine of unjustified tax benefit, which reinforces the anti- avoidance effect.

3 Judicial proceeding based on the concept of a "person with a beneficial ownership to income" until the emergence of national regulation

One of the first cases in the proceeding of Russian courts on the use of the concept of "a person who has a beneficial ownership to income" is the case that was considered in 2011 at the suit of company "Toros". [Federal District Arbitration Court: KA-A41/2465-11 (2011)]

In this particular case, the tax authority failed to prove the transitional nature of the entity's transfers to a foreign company in two circumstances, since the courts followed a formal legal approach into assessing applicable tax benefits. According to the court, the beneficial owner of income is the title

owner, therefore the possibility of applying benefits is carried out on the basis of a confirmed residence.

It is not clear from the content of the judicial act what evidence was submitted by the tax authority to confirm the transiting nature of operations, since the court only indicates the rejection of the argument of the corresponding tax authority, on top of that there were additional facts in favor of the applicant, such as: availability of loans issued from other companies, and availability of information provided by a foreign company regarding the payment of its taxes executed in their own state.

The following year in 2012, the arbitration court reviewed the dispute in the case of the applicant, of the foreign company "Eastern Value Partners Limited". [Arbitration Appellate Court: 09АП-33421/2012-АК (2012)].

Similarly, in this case the tax authority failed to prove the absence of the factual right to income. Regardless of that a certain level of progress can still be noted in the approaches of the tax authorities and the presented facts.

Based on a combination of circumstances, the tax authority concluded that the sole purpose of the transaction was precisely to minimize the taxation by obtaining benefits under an agreement with Cyprus.

According to the inspection, the beneficiary owner is an entity who is both a recipient of interest income and also has the disposal right on it. Only such entity can apply the agreement.

In support of its approach to understanding the concept of an entity who has the factual right to income used in the agreement with regard to loans, the tax authority referred to the explanatory letters of the Ministry of Finance of Russia, as well as to the comments to the OECD model convention.

By refusing the tax authority, the court proceeded from a formal understanding, based on the instructions of the tax authorities on the application of chapter 25 of the Russian Tax Code.

Hence, in the first court cases, it was demonstrated that at such stage, the tax authorities did not develop a standard of demonstrating these types of disputes, as well as a justification of the meaning of this concept for counteracting the abuse in the use of double taxation avoidance agreements.

The courts adhered to a formal legal approach and did not demonstrate an interest in the economic essence of transactions made by legal entities.

It should not be surprising that the next case that managed to reach the court appeared only in 2015, i.e. only after the proper definition appeared in the Russian Tax Code, which was preceded by a quite intense discussion among professionals and among the press.

Despite that, it can already be attributed to a notable turning point, since the tax authorities of this case were able to prove that the purpose was precisely that to obtain an unjustified tax benefit.

4 The judicial proceeding after the appearance of the new edition of Art. 7 in the tax code, but before its entry into force

We are referring to the case, in which the company "Equant" was the claimant. A dispute arose regarding the taxation of royalties through an agreement with Ireland. [Arbitration Appellate Court: 09АП-56340/2014 (2015)].

In particular, the following facts were put forward and confirmed in support of the groundlessness:

- The absence of the subject of the transaction, the intellectual rights (know-how);
- Affiliation and interdependence of the parties to the License Agreement and the consistency of their actions;
- Publicly known Information;
- Lack of commercial value of the transmitted Information;
- Further transfer of funds under the control of the parent company.

These findings were supported by expert opinion, analysis of reports of foreign companies, etc.

In the same year, there was an example of a case in which the inspectorates failed to prove the absence of the beneficial owner to income and the receipt of unjustified tax benefits. [Arbitration Appellate Court: N A14-13723/2013 (2015)]

In this case, in 2012, the company had to pay dividends to its only Swedish shareholder. In the opinion of the inspectorate, this company was not

the beneficial owner of income, since it transferred its income in full to a Swedish company, which was its sole shareholder. The tax authority supported its own position with the argument that the company received the shares of the Russian company as a contribution of its shareholder without any counter payment, and therefore did not bear the corresponding risks, and hence the company receiving dividends could not dispose of them. Nonetheless, the court found these arguments unproved by the tax authority and to be based only on mere assumptions.

Between 2015 and 2016, examples of relevant cases became more and more common.

Some cases can be classified as perfectly indicative of the collection of evidence by the tax authorities.

For example, the case of the company Capital [Arbitration Appellate Court: N 09АП-44501/(2016)]

An important feature of this case was that the tax authorities traced not only all operations up to the 3rd link, but also paid attention to their rhythm. Thus, the applicant Russian company contributed to the authorized capital of Cyprus' companies by transferring the shares of the PJSC "Severstal" in its possession in exchange for the shares of the said companies at an unequal value. Cyprus companies were created shortly before the operation and did not carry out economic activities. For a limited period of time, these Cypriot companies, through a series of related second-tier companies had transferred the disputed shares to firms registered in the British Virgin Islands. The courts found that in the initial transfer of shares from the Russian company there was no investment component, since the shares received by the Cyprus company were transferred to second-tier companies immediately on the next day. This means that such transaction covered a royalty-free transfer of shares to the final recipient registered on the British Virgin Islands.

In its decision, the court thoroughly analyzes the comments to the OECD Model Convention and concludes that these provisions of the comments clearly indicate that the actual owner of the income (the beneficiary) cannot be a company that performs, in relation to the income received, functions

related to the technical storage or transfer of the received income to another entity.

Thus, the court concluded that the taxation of paid dividends is based on the fact that the final beneficiaries receive income in an offshore jurisdiction (British Virgin Islands), with which there is no agreement on the avoidance of double taxation, so the tax is deducted and paid at the rate applicable by the Russian legislation.

Arbitration Appellate Court N A40-442/2015 (2016) – In this case, the court agreed with the conclusions of the tax authority, that the Swiss bank with respect to the disputed deposits was an agent (intermediary) who, on behalf of and at the expense of third parties (bearing all risks), placed the funds in the deposits. The actual beneficiaries (beneficial owners) of the disputed interests were represented by other entities (investors), and not by the Swiss bank itself.

At the same time, the Bank could not help but realize that the provided deposits by Credit Europe Bank S.A. (Switzerland) were not the bank's own funds (in relation to these deposits, the Swiss bank represents only the agency's (intermediary) functions) and that the interest is not actually paid to the Swiss bank, but directly to the other entities (investors).

Federal District Arbitration Court N A40-116746/2015 (2016) – In this case, the courts concluded that since the actual recipients of the disputed interest were other entities (investors), and not the Cyprus brokers (in respect to the disputed interest (agent) functions), then in this particular case, when these interests were paid, there were no legal grounds for applying the exemption (exemption from taxation in the Russian Federation) provided for by the Agreement for entities (for residents of Cyprus) who are the beneficial owners of interest income. (Applicant – MDM Bank, Public Joint-Stock Company)

Arbitration Appellate Court N A40-241361/15 (2016) – The court concluded that ISPH was not the beneficiary of the interest received, but acted as an intermediary used by the shareholders, ISM and the Bank, to abuse the tax law and to obtain an unjustified tax benefit in the form of an interest rate reduction up to 0 % according to art. 11 of the Agreement (Russian

Federation – Luxembourg), therefore, the bank did not have the right to apply a preferential 0 % rate between 2010 and 2011 when paying interest on loans, attracted by "KMB Bank" at the expense of funds in common with the shareholder's bank, in accordance to the Art. 11 of the Agreement of 28. 6. 1993 between the Russian Federation and the Grand Duchy of Luxembourg regarding the avoidance of double taxation and the prevention of tax evasion with concern on taxes on income and property. The limited nature of ISPH's brokering activities and the issuance of loans by this holding company at the expense of funds in common with the shareholder's bank does not allow, for the purpose of applying a 0 % preferential rate, to recognize ISPH as a beneficiary (actual interest holder) who actually acted as an intermediary for ISM (Italy) and was used by the controlling shareholder of the bank for the purposes of non-payment of income tax to the federal budget of the Russian Federation at a rate of 10 %, since the bank, being a tax agent, did not withhold the aforementioned taxes.

In the case of Arbitration Appellate Court No. A03-21974/2017 (2018), the concept of the beneficial income owner was applied to prove the fictitiousness of the transaction. The court noted that the foreign shareholder, having limited powers with respect to disposing of the income received, having an absence of any operations that caused economic activity, not actually benefiting from the income received and not determining its subsequent fate, respectively could not be even considered as having actual right to income. At the same time, the Russian company acting as a tax agent was charged with unjustified tax benefit in the form of evading the execution of the duties of a tax agent.

The proceeding of reconstruction carried out by the tax authorities finally began to take shape. For example, in Federal District Arbitration Court, No. A11-9880/2016 (2018), the tax authorities, after determining the beneficial ownership of income, recalculated the rate based on the agreement of the residence country of the beneficial owner of income.

An interesting proceeding began to take shape at the level of the Supreme Court of the Russian Federation in relation to the national rule on thin capitalization. In the opinion of the court, the retraining of interest into dividends should have led to the possibility of applying the relevant articles

of the agreements on the sole basis of such retraining, however the court has now commented on this issue and has taken into account the concept of an entity with a beneficial ownership to income. For example, in case of the Supreme Court of the Russian Federation N 304-KG17-8961/2018 (Supreme Court of the Russian Federation N A40-176513/2016/2018).

The Supreme Court of Russian Federation additionally noted that according to the OECD Comments to Art. 10 of the model convention, the term "beneficial owner of income" should not be applied in a strictly technical sense, but should instead be understood on the basis of the goals and objectives of international treaties for the avoidance of double taxation and taking into account such basic principles as preventing the abuse of contractual clauses and the prevalence of substance over the form. Particularly, granting exemption from paying taxes at the source of the income payment is simply incompatible with the goals and objectives of the Model Convention in the case in which the resident of another state that is receiving income acts as a nominee for another subject who is actually the beneficiary of the income under question. Therefore, Art. 10 of the Agreement cannot be applied when the relations behind the provision of financing and income payment are not connected with attracting foreign capital to the Russian economy, and the actions of the participants in these relations are aimed only at creating a convenient (preferential) tax regime. In such situation, taxation is made by taking into account the tax residence of the beneficial owner of income.

The approaches in determining the entity with the actual right to income, which were developed in the judicial acts between 2015 and 2017 and also early 2018, allowed the tax authorities to issue a letter summarizing these proceedings and formulating the substantive conclusions that will be actively used by the tax authorities in their work. (Russian Federal Tax Service: CA-4-9/8285/2018)

These findings were sharply criticized by the scientific community, since the tax authorities passed conclusions:

- about the general, rather than exclusive, nature of the concept of an entity with a beneficial ownership to income in the context of combating abuse;

- that in matters of proof, it is necessary to make a shift in the direction of the reality of business activities carried out by a foreign company, against the approach to the assessment of the powers to manage income and the taken risks.

5 Judicial proceeding using the new version of Art. 7 of Russian Tax Code

The judicial proceeding using the new version of Art. 7 of the Russian Tax Code so far only applies to the issues of determining the periods to which the new edition of this article may apply.

For example, Arbitration Appellate Court N A27-13314/2018 (2019) indicated that the new edition of Art. 7 got recognized by the court as permissible because the legal value does not stand for when the decision was merely made to make a contribution to the company's property (2014), but to when the contribution had actually taken place (in terms of credit for loan obligations, 2015).

Simultaneously, it should be noted that with the issues of determining the entity with a beneficial ownership to income, the Federal Tax Service monitors the acts of the smaller tax authorities. According to information from the Federal Tax Service in 2018, more than half of the acts sent to the Federal Tax Service of Russia did not receive an approval (the absence of the beneficial ownership to income was not confirmed), some of the acts were sent for a revision because the standard of proof was not met and the territorial authority needed to take additional measures of tax control. The taxpayers (tax agents) voluntarily agreed with some conclusions and filed updated declarations. Only a small part of the cases was then taken to court.

Thus, the proceeding of tax authorities is formed not only through court, but also at the pre-trial stage. The Federal Tax Service seeks to ensure a certain level of standard of the application of this concept and corrects the findings of smaller-level tax authorities that do not correspond to it or for which they already had put together an unambiguous judicial proceeding.

Trying to solve these issues only on the domestic level tends to be ineffective, given that globalization of economic activity undermines local legislative interventions and requires a more harmonious and shared action. In light of this scenario, one realizes the importance of supranational bodies in the study of Exchange of Information on tax matters and the formulation of proposals that can be implemented jointly by the international community (Estellita, Bastos, 2015: 15).

Last year, automatic exchange of tax information was firstly launched. This information in the near future will already be able to be used by tax authorities in their work and how effectively it will be implemented also reflects the number of legal disputes.

In the future, the results of the work of the tax authorities will be visible.

6 Prospects and problems

One of the most important matters to a taxpayer is the certainty of their situation, the range of the responsibilities placed upon them and the rights they were given in relation to the establishment and payment of the tax [Drywa,2017: 290]

Legal norms despite their abstractness should precisely indicate to the manner of behaviour of the entities. There should be no doubt what is the appropriate behaviour of particular entities. The formal certainty of tax law should enable an appropriate organization of their tax-law relations through a precise outlining of their rights and responsibilities towards the state in terms of payment of taxes (Juchniewicz, Stwoł, 2017: 306).

As of now it becomes clear that the development of the concept of an entity with a beneficial ownership to income is nearly impossible without taking into consideration also the international experience.

References to the OECD approaches at first seemed rather exotic in matters of this kind, but now it has become routine and it stopped causing any stir.

The active participation of tax and financial authorities of Russia in conferences on countering tax evasion and erosion of the tax base allows them to quickly learn the best proceedings and implement its practice.

The introduction of the BEPS plan into the proceeding of tax authorities around the whole world reinforces the relevance of this concept.

But there are also problems that are caused precisely by regional development, which leads to the fact that each government forms its own approach and definition.

The development and implementation of the BEPS plan gives this evolution a new impetus, making for a new look at seemingly well-known truths. And numerous and sometimes heterogeneous interpretations of the concept by courts and tax authorities continue to produce risks in terms of both double taxation and the total absence of taxability of cross-border income (Demin, Nicolaev, 2019: 13).

The Multilateral Convention to Implement Tax Treaty Measures to Prevent Base Erosion and Profit Shifting or Multilateral Instrument (MLI) has been described as "an historical turning point in the area of international taxation" which introduces a third layer of tax rules for the taxation of cross-border transactions in addition to domestic tax law and bilateral tax treaties (Duff, 2018).

There are several good reasons for developing countries to sign the MLI (Oguttu, 2018: 4):

- The tax treaty-related BEPS measures set out in the MLI have the potential to reduce vulnerability to tax planning strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations where there is little or no corresponding economic activity.
- The MLI is designed so that it can modify any DTA, whether is based on the OECD or the UN Model Conventions.
- The MLI can strengthen source taxation, especially by addressing treaty shopping, and abuse of the taxable presence requirement in the definition of a permanent establishment (PE).
- The provisions can preserve source taxation by ensuring that profits are taxed where the economic activities generating those profits are performed and where value is created.
- Considering the costs and time involved in re-negotiating treaties, the MLI provides the easiest and less costly method of updating

treaties. Reliance on bilateral negotiations to introduce the BEPS measures would cause uncertainties, delays and expenses and would tend to disadvantage developing countries.

These reasons indicate that the future is in international cooperation.

On the 17 April 2019 The State Duma of Russia adopted a law on ratification of a multilateral convention on the implementation of measures relating to tax agreements in order to counteract the erosion of the tax base and the withdrawal of profits from taxation (concluded in Paris on 24 November 2016) (MLI). What does this mean for the development of the concept of beneficial ownership?

Although Russia included agreements with 71 countries on the list, some of the countries on the lists did not sign the agreement, and some of the countries on this list adhere only to the main goal rules. Nevertheless, we presume that the implementation of this convention will create certainty in the approaches of the tax authorities of different countries.

7 Conclusion

The number of disputes over the determination of whether or not an entity has a beneficial ownership to income shows that it is too early to talk about the existence of a formulated concept, on the contrary, we are still far away from the completeness of the discussions on the issue.

The hypothesis about the stages of development of the concept under consideration was confirmed on the basis of the emerging judicial proceeding.

In the process of studying the evolution of this concept, it becomes clear that now the tax authorities and the courts in the Russian Federation are halfway there into forming an understanding of the concept of an entity having an ownership on income.

New opportunities for tax control and the amount of information will allow to obtain reliable information about the activities of all companies in the relevant chains, to identify the relationship between them and the interdependence of their actions and transactions. This will help sharpen the criteria for an entity with a beneficial ownership to income.

Tax administration should be expressed not in the opposition of the taxpayer to the tax authority, but in their interaction and cooperation. The shift to the partnership model of tax administration contributes to its optimization in terms of budget expenditures and administrative costs, allows to reduce the total number of tax disputes, and gives taxpayers confidence that their tax strategies correspond to the letter and spirit of the law [Demin,2018: 28]

At the same time, it is possible to predict the growth of the relevant disputes, when tax authorities attempt to expand the use of this concept in the general sense of the doctrine, into obtaining unjustified tax benefits and taking into account the reality of the activities of a foreign company, and their reduction after reconfiguration and adaptation of companies to these new rules, subject to their universality and consistency. Thus, it is necessary to move away from purely national formulations, yet still strive to create a unified concept at the international level, which is greatly facilitated by the implementation of the BEPS Project and MLI.

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Peculiarities of Public Finance Management in the Sphere of Higher Education in the Russian Federation

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Abstract

The paper deals with the effects of the changes in statutory regulations regarding the provision of finances for the execution of government orders and discusses the developments in the procedures for the calculation of subsidies. The objective of this study is to make a review of the nature of public finance management in the sphere of higher education in the Russian Federation. The latest developments in the legislation regulating the activities of higher education establishments have altered the environment in public institutions and enabled the creation of legal and financial practices aimed at the improvement of quality and availability of federal and municipal services, as well as for the efficiency of assets management in public institutions.

Keywords: Government Order; Per Capita Financing; Cost Group; Adjusting Factor.

JEL Classification: H20; H57; I23; P46.

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1 Introduction

Bierbrauer and Boyer (2016) notice that there are different models in normative and positive public finance. From this reason, it is difficult to provide answers to the following questions: does political competition generate Pareto-efficient outcomes? Does it generate welfare-maximizing outcomes? Is there a sense in which political competition gives rise to political failures, in analogy to the theory of market failures?

The need for the enhancement of vocational education contributions to the social, economic, and cultural modernization of the Russian Federation, as well as the growth of competitiveness in the global market, requires an increase in the efficiency of state funded, independent, and municipal, educational institutions. It also requires the introduction of transparent funding mechanisms and practices for the encouragement of innovations offered to higher education establishments.

Changes in the legislation that affects the activities of higher education establishments have altered their economic environment dramatically. They have also provided for the development of legal and economic solutions that contribute to the improvement of quality and availability of federal and municipal services and the efficiency of utilization of the assets under ongoing management by state agencies.

Two examples of such solutions are the modernized system for the funding state and independent institutions and the increased economic independence of subordinate institutions in the course of executing government orders.

2 Financing the Execution of Government Orders

According to the latest amendments concerning public services, the Budgetary Code defines a government order as a document stipulating the scope, quality, structure, and the criteria for acceptance of the implementation.

Government orders are used by the Ministry of Science and Higher Education of the Russian Federation for managing the funding of statutory activities

at subordinate educational institutions, as the ministry is the founder and the supreme executive authority for higher education establishments.

The government of the Russian Federation has developed regulations regarding the procedure for the provision of government orders for public services (works). These regulations specify the list of public services and the manner of their funding for federal institutions. The senior budget holder creates a government order in compliance with the approved institutional list of public services and works provided and performed by specialized federal establishments, which is formed based on a list of basic federal and municipal services and works. Such a list is developed and approved by the federal executive authority engaged in the process of elaborating federal policy and statutory regulations relating to the approved activities.

The government of the Russian Federation has formulated and approved the rules for the development of basic lists and lists for specific industries/sectors. As per the resolution of the government of the Russian Federation, register entries with unique registration numbers must be made for the information associated with any Federal (municipal) service. In its turn, the Ministry of Finance of the Russian Federation has formulated and approved the order of formation and amendment of register entries in the process of creation and management of basic lists and lists for specific industries/sectors. Register entries are made and stored in digital format in *Electronic Budget*, an integrated state information system for public finance management.

The application form for government orders was approved by the resolution of the government of the Russian Federation #640 of 26 June 2015, "On the procedure for issuing government orders to federal institutions for the provision of public services (performance of works), and on the order for funding the execution of government orders". Besides the name of the public service and absolute and qualitative indicators, this form provides information related to the unique registry entry for each service, as well as the details concerning the scope and the terms of provision of the public services. The order form now contains information about any allowable deviations from the target values in terms of scope and quality of the services provided. The list of quality indicators for public services provided

by higher education establishments has been approved by the order of the Ministry of Science and Higher Education of the Russian Federation. The order specifies the indicators of quality of public services related to higher education, including the following: grade point average of the students enrolled in a program (course) with due allowance for the mode of attendance; passing grade of the students enrolled in a program (course) with due allowance for the mode of attendance; proportion of the graduates (by specialty) who found employment after graduation; and the proportion of the graduates (by specialty) who found employment after graduation and have at least three years of work experience in line with their areas of specialization.

If we consider the statistics for the funding of higher education establishments in Voronezh Region over the past three years, we will see that the amount of funding strongly depends on the number of students enrolled in the various programs.

When it comes to higher education services, the amount of public services provided depends on the number of students.

The tables below show the statistics for the financial provision of Government orders.

Table 1: Funding of higher education establishments subordinate to the Ministry of Science and Higher Education of the Russian Federation in Voronezh Region in 2016

Index	Voronezh Region					
	Voronezh State University of Forestry and Technologies	Voronezh State Pedagogical University	Voronezh State Technical University	Voronezh State University	Voronezh State University of Engineering Technologies	Total for the region
Total number of students (excluding basic, supplementary and supplementary vocational education)	1 593,60	2 749,30	10 147,30	8 468,75	3 474,25	26 433,20
Subsidy for Government orders, total, thousand rubles	158 618,70	215 001,60	1 008 576,60	892 663,70	295 032,10	2 569 892,70
Subsidy for educational activities	130 221,00	202 145,40	829 152,30	677 696,50	275 469,70	2 114 684,90
Subsidy for service provision	-	33,40	27 626,10	42 721,80	100,10	70 481,40
Subsidy for upkeep of property	2 651,40	7 070,20	25 960,40	31 900,40	5 716,40	73 198,80
Subsidy for Government order performance	746,30	5 752,60	23 753,40	59 812,90	13 745,90	103 811,10
Subsidy for the provision of services associated with education and youth policy	25 000,00	-	102 184,40	80 532,10	-	207 716,50
Subsidy for other purposes, total, thousand rubles	59 513,60	116 267,60	396 610,10	382 895,20	126 381,20	1 081 667,70

Table 2: Funding of higher education establishments subordinate to the Ministry of Science and Higher Education of the Russian Federation in Voronezh Region in 2017

Index	Voronezh Region					
	Voronezh State University of Forestry and Technologies	Voronezh State Pedagogical University	Voronezh State Technical University	Voronezh State University	Voronezh State University of Engineering Technologies	Total for the region
Total number of students (excluding basic supplementary and supplementary vocational education)	1 479,40	2 537,30	10 179,10	8 661,95	3 360,35	26 218,10
Subsidy for Government orders total thousand rubles	180 399,30	227 550,20	991 452,60	959 154,70	313 898,00	2 672 454,80
Subsidy for service provision	-	-	30 355,80	47 263,00	-	77 618,80
Subsidy for upkeep of property	2 464,50	6 264,50	25 842,00	29 708,10	5 386,90	69 666,00
Subsidy for Government order performance	9 000,00	10 272,20	16 210,20	48 518,10	9 827,80	93 828,30
Subsidy for the provision of services associated with education and youth policy	25 000,00	2 000,00	7 157,40	30 700,00	-	64 857,40
Subsidy for other purposes total thousand rubles	72 844,80	92 689,20	411 702,30	350 557,40	102 570,00	1 030 363,70

Table 3: Funding of higher education establishments subordinate to the Ministry of Science and Higher Education of the Russian Federation in Voronezh Region in 2018

Index	Voronezh Region					
	Voronezh State University of Forestry and Technologies	Voronezh State Pedagogical University	Voronezh State Technical University	Voronezh State University	Voronezh State University of Engineering Technologies	Total for the region
Total number of students (excluding basic supplementary and supplementary vocational education)	1 507,10	2 407,60	10 021,95	8 639,50	3 278,95	25 855,10
Subsidy for Government orders total thousand rubles	194 148,90	276 184,80	1 191 568,20	1 103 133,10	389 060,10	3 154 095,10
Subsidy for service provision	-	-	39 818,10	64 925,50	-	104 743,60
Subsidy for upkeep of property	2 128,50	10 227,90	30 257,10	29 536,40	5 617,80	77 767,70
Subsidy for Government order performance	14 516,90	10 308,20	24 210,80	51 146,90	9 827,80	110 010,60
Subsidy for the provision of services associated with education and youth policy	-	-	17 554,20	30 000,00	-	47 554,20
Subsidy for other purposes total thousand rubles	71 765,40	119 248,00	376 025,60	450 448,40	105 419,30	1 122 906,70

When it comes to higher education services, the amount of public services provided depends on the number of students. As the amount of funds allocated to the educational establishment for the purpose of execution of government orders depends on the scope of the public service being provided, the methods of assessment of the number of students acquire greater significance. The complexity of estimating the scope of provided public services in the sphere of higher education has to do with the fact that the academic year is different from the financial year and the duration of training courses are more than a year. At present, the scope of public services associated with higher education is estimated by the Ministry of Science and Higher Education of the Russian Federation for the financial year by way of calculating the average number of students per year with due

account for the expected number of students admitted and graduated. The subsidies for the provision of finances for the execution of government orders are allocated from the respective budgets (Endovitsky, Galchina, Korobeinikova, Panina, Sapozhnikova, 2018: 124–128). They are calculated based on public services indices, in compliance with the government orders, and with due account for standard costs associated with the provision of those public services, as well as for standard costs associated with the upkeep of the properties of federal and independent institutions.

Besides the provision of public services, educational institutions also perform research work, provide expert assessments, organize public events, and carry out other works associated with government orders. One of the key characteristics of the aforementioned works is the absence of standard costs per unit. For this reason, such works are normally funded based on project estimates. The costs, which are calculated in compliance with the order from the Ministry of Science and Higher Education of the Russian Federation, as well as the study of financial feasibility of the works, are included in the subsidy for the execution of the government order. Currently, a subsidy for the performance of a government order includes the costs associated with the upkeep of properties, including a portion of the taxes on the property owned by the institution (Endovitsky, Gerasimov, Kostukova, 2015: 85–87).

The funds allocated for the execution of government orders for public services cover operating expenses and are not related to the capital costs. Budget allocations for development purposes are made in the form of capital investments in state-owned assets and subsidies provided for other purposes. Higher education establishments have the right to spend the funds provided as a part of a subsidy for execution of a government order with the condition that it does not compromise the quality of the services provided.

A subsidy for the execution of a government order is formed by the sponsor and provided to the institution based on an agreement regarding the terms of allocation of such a subsidy.

3 Per Capita Financing of Educational Programs: Key Principles and their Consequences for Higher Education Establishments

Currently, state educational institutions are funded in accordance with the principles of per capita financing of educational programs. The assessment of the funds required for the provision of public services is based upon the standard costs that are common for all higher education institutions. These standard costs are classified by specialties and training programs.

The need for the transition to the use of standard costs in the assessment of funds allocated for the performance of public services was specified in the order of the President of the Russian Federation #599 dated 7 May 2012 "On national policy measures in the sphere of education and science". In compliance with this order, the Federal Government was authorized to organize the transition to per capita financing of higher vocational education programs, as well as to provide for a growth in the funding of leading educational establishments that are training specialists in the field of engineering, medicine, and science. The norms of funding were calculated with due regard for the implementation of educational programs.

Per capita financing provides a strong link between the amount of funding allocated with the number of students. The transition to per capita financing signifies the creation of standard transparent norms of funding educational programs, as well as the abandonment of the practice of financing educational establishments regardless of their efficiency and quality of the services provided. The basic principles of the per capita financing system have been described in the methods for estimating standard costs for the provision of public services associated with the implementation of higher education programs for accredited specialties, which were developed and approved by the Ministry of Science and Higher Education of the Russian Federation in 2015.

Per capita financing methods allow for the differences in human resources and tangible assets that have most influence on the cost of various training programs (Krivosheev, 2017: 139). These differences are associated with the complexity of training, which is determined by the proportion of teachers and students, as well as by the requirements for teaching staff; the need

for extra staff for some programs (e.g. additional laboratory assistants); the need for laboratory equipment and utility infrastructure; the nature of internships; etc.

The basic components of the per capita financing system are the cost groups determined for specialties and training programs, basic standard costs, adjusting factors, which influence the value of the basic standard costs. Basic standard costs are the minimum values of the standard costs of provision of a unit of educational services to intramural students, which are determined for each cost group of specialties and training programs. Cost groups include specialties and training programs that are combined in integrated groups of specialties and training programs. Cost groups for various specialties and training programs are formed with due regard to the basic requirements for the implementation of educational programs, such as the requirements for facilities and equipment, including the utility and support infrastructure, materials, technical and methodological support of the program, human resources, etc. There are three cost groups based on their complexity and the specifics of the services provided.

An important role in per capita financing system is played by the adjusting factors approved along with the list of cost groups and basic standard costs. The use of adjusting factors provides an opportunity to consider the objective factors determining the differences in the cost of providing educational services that are neglected when forming cost groups (Panina, 2010: 101). Adjusting factors are applied to some components of basic standard costs. Adjusting factors represent an important tool when it comes to implementing federal policy in the sphere of higher education. Certain factors are used when reporting on types of education and technologies, as well as on the nature of particular training programs. There is a separate group of factors provided for reporting on the objective characteristics of higher education establishments as a whole. Such factors include: geographic location; the right of the higher education establishment to approve educational standards of its own; and the ability to provide educational services to students with disabilities (Svetashova, 2016: 192).

The adjusting factors related to the geographic location of the establishment have to do with the fact that the average salary of the teaching staff

must be in line with the average pay in the respective region, as per the order of the President of the Russian Federation. To estimate the amount of funding allocated for the purpose of implementing government orders by a particular higher education establishment, the basic standard costs of providing public services (determined for the cost groups by specialties and training programs) are to be multiplied by the scope of public services (determined for specialties and training programs) and by the adjusting factors determined for the modes of attendance (evening classes, extramural, etc.). Other factors include the network of the implemented educational programs, educational technologies (remote, electronic), and objective characteristics of the groups of educational establishments. In addition to the aforementioned factors, it is necessary to observe the financial restrictions imposed by the federal budget for the current year on the funds allocated for implementing government orders (Endovitsky, 2018: 258).

The methods adopted describe the general rules for the formation of the per capita financing system. They do not provide for any particular values of standard costs and adjusting factors, or for the number and composition of the cost groups. The methods represent a framework document, allowing for the annual determination of the basic components of per capita financing (Endovitsky, Polukhina, Korobeynikova, 2018: 113). Both, basic standard costs and adjusting factors are subject to alterations depending on the changes in the standards of education, policy priorities, and budget constraints. This ensures the flexibility of the per capita financing system, its adaptability to changes in educational standards, and the emergence of new specialties and technologies of education. The modeling and analysis of different methods of transition to per capita financing, which were developed for educational establishments, provides an opportunity to choose the mildest scheme for a phased transition. At first, a hybrid scheme of financial provision was applied. The amount of funding of higher education establishments was partly determined in compliance with the uniform standards developed for specialties and training programs, and partly based on the individual standards adopted by each particular establishment. By 2016, the educational services provided to around 80 % of the students pursuing bachelors', specialists' and masters' degrees, and more than 90 %

of postgraduate students were financed in accordance with the standard costs approach. The transition to the per capita financing of higher education establishments subordinate to the Ministry of Science and Higher Education of the Russian Federation was completed by 2017. The phased transition to the new method of funding has proved to be the best option. Starting with 2017, the Ministry of Science and Higher Education of the Russian Federation has been setting unified basic standard costs. Not only for subordinate higher education establishments, but also for all educational institutions taking part in tenders for the provision of publicly funded educational services in accordance with the accredited higher education programs, regardless of their subordination and the form of ownership.

4 Conclusion

Among the challenges faced by the higher education establishments that have undergone the transition to per capita financing, regardless of their subordination, we must mention the need for improvements in the existing standards. For instance, the expansion of the list of items to be funded in the context of the implementation of government orders (e.g. funding the hall of residence, tax reimbursement) could have a positive impact on the process of providing public services.

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Uncertain Legal Status of the Central Bank of Russia

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Abstract

This article is devoted to the scientific and practical study of the legal provisions governing the status of the Central Bank of the Russian Federation. The comparative analysis of the foreign practice of the activities of this institution is made. The genesis of the studied institute is considered. The main objective of this work is to draw conclusions about the independence of the Bank of Russia and its belonging to the state authorities. The following scientific methods were used: analysis and synthesis, generalization, deduction, analogy, as well as a systematic approach to the objects of study.

Keywords: Central Bank of the Russian Federation; State Authorities; Legal Status; Emission of Currency / Cash Issue; Monetary Policy.

JEL Classification: O17.

1 Introduction

The article discusses the actual practical topic from modern Russia. Currently, there are heated discussions about the belonging of the Russian Central Bank to the state authorities and, at the same time, about the independence of this organization from all branches of government. The purpose of this work is to determine the legal status of the main Bank of Russia, as well as its comparison with similar institutions in foreign countries. The author leans towards the view that the Central Bank is close in its powers to the activities of the state authorities. For this study, the following methods of scientific

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knowledge were used: analysis and synthesis, generalisation, deduction, analogy, as well as a systematic approach to the objects of study. The following authors have previously written on this topic: Arzumanova L., Bratko A., Vikulin A., Veshkin Yu., Geyvandov Ya., Glukhovsky Ya., Glushko A., Gracheva E., Dzyavgo D., Efimova L., Kosikovsky C., Rozhdestvenskaya T., Oleinik O., Pastushenko E., Stolyarenko V., Tavasiev A., Topornin B., Tosunyan G., Chebykina N., Chernikova E., Ekmalyan A. and others.

2 Formation of the Institute of the Central Bank in Russia and foreign countries

2.1 The development of the legal status of the main banks in foreign countries

In foreign countries, the main national banks have different names, for example, state, national, issuing, reserve, like in particular, the National Bank of Poland, the Federal Reserve System (USA), the Bank of England, the Bank of Japan, the Bank of Italy, Deutsche Bundesbank (Germany), etc. (Arzumanova, 2012: 50–55; Dziavgo, 2005: 287; Glushko, 2008).

Initially, the functions of exchanging, storing, and accounting for money were performed by church institutions (Arzumanova, 2012: 50–66). Gradually, with the development of commodity-money relations, with the appearance of a minted coin, some monetary transactions were carried out by special financial intermediaries, whose activities were strictly regulated and controlled by the state, actually these were the first banks. In the late XIX–early XX century, in most countries, the largest banks began to cooperate with state authorities. Subsequently, they received the exclusive right to issue public funds and began to perform control and supervisory functions in relation to other credit institutions. It is believed that the first central bank was the Bank of Sweden – Riksbank, founded in 1668.

Central banks arose as commercial banks with the right to issue banknotes. Despite the fact that the first bank to issue was the Bank of Stockholm (in 1650, it issued deposit certificates for gold coins, which were issued to the bearer and were treated like other types of money throughout the Kingdom of Sweden) (Arzumanova, 2012: 50–55), the Bank of England, established

in 1694, is considered to be the first issuing bank, since it began to issue banknotes and take into account commercial trade papers. The process of mass creation of such banks dates back to the beginning of the XIX century. So, in 1800, the Bank of France was created, in 1814–the Bank of the Netherlands, in 1816–the Austrian National Bank, in 1817–the Bank of Norway (Glushko, 2008). Throughout the nineteenth century, they carried out ordinary banking operations and the only thing that distinguished them from private banks was the exclusive rights to issue money and the resulting special relationship with the government.

Later, in addition to issuing banknotes, the role of the state treasurer and the intermediary between the state and commercial banks, and the organization that implements the monetary policy of the state was entrusted to central banks.

Central banks were nationalized, and now the capital of these banks is wholly or partially owned by the state.

Thus, in 1718, the Bank of England began to control the issue of government securities, and in 1844 it received a monopoly right to bank issue. The Bank of England was the lender of last resort for all other lending institutions that kept their reserves with the Bank of England. In 1946, the Bank of England was nationalized (Arzumanova, 2012: 50–55).

In many states, a two-tier banking system is established, in which the central bank and control (supervisory) financial bodies are at the highest level, and at the lower level there are commercial lending institutions, their associations and unions (Veshkin, Avagyan, 2004: 11).

The central banks of foreign countries differ in the degree of independence in decision making. It depends on the established relationship between the central bank and the national government. Other factors are state participation in the capital of the central bank and in the distribution of profits (may not have a particular impact on the independence of the bank); the procedure for appointing the management of the bank, who is able to influence the degree of political independence of the bank from the authorities; the degree of reflection in the legislation of the goals and objectives of the central bank. In countries such as Austria, Germany, Denmark, Poland,

Russia, France, Switzerland, Japan, the Netherlands, the main goals, objectives and scope of the central bank's activities are reflected in the constitution and (or) are set out in the laws on central bank or banking (Arzumanova, 2012: 50–55; Dziavgo, 2005: 287). In the USA, Sweden, Italy, for example, the tasks of the central bank are formulated only in general terms.

It is also an important factor to allow the state to intervene in monetary policy. For example, the legislation of Great Britain, the Netherlands and Sweden clearly establishes the possibility of state influence on the policies of the central bank, including the rights of state bodies to override a bank's decisions. In many countries, the external state control over the activities of the central bank in the area of monetary policy is provided. For example, in Poland a proposal was made to introduce the institution of the Commission on Banking Affairs at the constitutional level. This offer was not accepted. However, the very idea of restricting the sole authority of the Chairman of the National Bank (appointed and removed from office by the Seim on the proposal of the President of Poland) was recognized and was implemented in the form of the Monetary Policy Council, whose members are chosen by the Parliament (the Seim and the Senate), as well as the President of Poland (Kosikovsky, 2005: 306).

The legislation of Austria and Denmark does not contain the formal right of the state to intervene in the relevant policies of the central bank, but obliges banks to coordinate their strategy according to the planned policy of the government of the country.

One of the most independent are the central banks of Germany and Switzerland, since the laws of these countries do not prescibe the right of the state to intervene in the monetary policy of the central bank.

Another factor affecting the independence of banks is the rules governing the possibility of direct or indirect financing of public spending by the central bank. Such a system has become widespread in most countries of the world. The exceptions are the United States and the United Kingdom, where government loans are distributed on the open market (Arzumanova, 2012: 50–55).

Central banks in Europe were created to establish control over monetary policy and ensure price stability. Later, in many countries, central bank control began to control the entire economy of the state, and this is the reason why in the middle of the twentieth century, most banks were nationalized. However, already in 1980–1990, there was a rejection of the state's total control over central banks, and the independence principle of these banks became one of the fundamental principles determining their legal status.

Generally, the banks reporting to the country's parliament (Germany, Holland, Poland, USA, Switzerland, Sweden) have greater autonomy, unlike those banks that report to the government (the majority in world practice).

In most cases, the central bank is owned by the state. If the state owns the capital of the bank (for example, in the USA, in Italy, in Switzerland) or partially (for example, in Belgium 50 %, in Japan 55 %), then it should be stated that the central bank performs the functions of an state authority because it exercises its powers representing the state interests, and pursues the policy in its interests (Stolyarenko, 1999).

A number of authors point out the following tasks facing the central bank of any country: 1) it issues the currency, 2) it is a bank of banks, 3) it is a government banker, 4) it is recognized as the main clearing centre of the country, 5) it manages the state economics by monetary methods. The author of the Russian concept of public law regulation of banking activity, Professor E. Chernikova, considers the Bank of Russia as a highly efficient banking regulator with sufficient administrative, economic and status independence. (Chernikova, 2009: 89–90).

2.2 Genesis of the Central Bank of the Russian Federation

The State Bank is the main bank of pre-revolutionary Russia – was established in 1860 on the basis of the reorganization of the State Commercial Bank. This institution was a governmental organization. The fixed capital originally allocated from the treasury was 15 million rubles, the reserve capital was 3 million rubles.

The scientific literature notes that the creation of the State Bank was preceded by almost a century of experience in the operation of state and

individual private credit institutions, which, against the background of social transformations in the society, were associated primarily with the abolition of serfdom, forced the government to change the state monetary policy in terms of banking affairs (Chernikova, 2008: 47–51). According to the Charter of the Bank from1860, the State Bank was created to "revive trade turnover" and "strengthen the monetary credit system" (Arzumanova, 2012: 55–60; Glushko, 2008). But the main part of the bank's resources at the first stage of its development was absorbed by direct and indirect financing of the treasury, as well as of the operations to liquidate pre-reform state banks. As an organ of governmental economic policy, the State Bank took an active part in the creation of the banking system of Russia. With its support, joint-stock banks and mutual credit societies were created later (the official site of the Central Bank of Russia).

According to the Charter, the State Bank was an institution reporting to the Ministry of Finance and was under the supervision of the Council of State Credit Establishments. The management of all operations and affairs of the bank and the supervision of their production was entrusted to the Board of the bank, which consisted of the Governor (chairman), his comrade (vice-chairman), six directors and three representatives from the Council of State Credit Institutions. Under the Board of the State Bank, there was an Accounting and Loan Committee, which consisted of the Bank Manager, his comrade, two bank directors and four members from the merchants. The committee was chaired by a bank manager.

On 6 June 1894, a new Charter was adopted. The main activity of the State Bank was to be intensive lending to trade and industry, especially agriculture. The basic capital of the bank was increased to 50 million rubles, the reserve funds – to 5 million rubles.

The new Charter introduced changes to the organization of management of the Bank. The State Bank was removed from the supervision of the Council of State Credit Establishments and was placed under the supervision of the State Control. The overall management of the State Bank was entrusted to the Board, which replaced the Board, and to the Bank Manager. The Council included the Director of the Special Chancellery for the credit unit, a member from the State Control, comrades of the Bank's manager,

the Governor of the St. Petersburg office of the Bank, members from the Ministry of Finance (their number was not limited), one member from the nobility and one from the merchants. The Chairman of the Council of the State Bank was its Governor.

A year after the approval of the Charter, the monetary reform started in Russia, and ended in 1898. In the course of this reform, the State Bank became the issuing center of the country on the basis of a decree of the emperor of 29 August 1897. Further, its main task was the regulation of money circulation. The bank was obliged to ensure the stability of the new monetary system. Up until the First World War, Russia's financial policy highly valued the preservation of the gold currency as the basis of an external state loan. The gold rate of the ruble was constantly maintained at a very high level. As noted in the scientific literature, the State Bank in the Russian Empire did not acquire the legal status of a central bank with corresponding oversight functions in relation to both credit institutions and the monetary circulation system as a whole. Even after it became issuing, in contrast to the central banks of other capitalist countries, the State Bank of Russia still remained the largest commercial bank that carried out large-scale lending to the country's economy. It did not manage to get rid of government dependence, to gain the status of an independent central bank in its activities. (Bartsits, Bykov, Chernikova, 2017: 33–34).

7 November 1917 the history of the State Bank ended. And the history of the People's Bank of the RSFSR began. In December 1917, the Soviet government started the reorganization of the country's credit system. After the armed seizure of the buildings of the Petrograd banks, a state monopoly on banking was introduced in the whole country. Joint-stock commercial banks and private banks were subject to nationalization and merger with the State Bank. Since January 1918, the Bank was renamed into the People's Bank of the Russian Republic, then into the People's Bank of the RSFSR.

The People's Bank of the RSFSR was part of the financial department of the People's Commissariat of Finance. Formally, until its abolition, the Bank operated on the basis of the statute of the State Bank of 1894, with a number of changes made.

In the second half of 1918, all payments between business organizations began to be made by means of checks or through an accounting transfer from the account of one organization to the account of another organization in the People's Bank of the RSFSR. At the end of 1918, under the supervision of the People's Bank of the RSFSR were transferred the Credit Office and the Expedition of the preparation of state papers, and in 1919 – the Treasury, its local bodies and the national savings banks as well. The Bank established the Budget Department to compile a state list of income and expenses. And when the Central Income and Funds Office was transferred to its supervision, the merger of the Central Administration of the People's Bank of the RSFSR and the State Treasury Department ended. As a result, the People's Bank of the RSFSR almost completely absorbed the former Ministry of Finance.

In early 1919, the People's Bank of the RSFSR ceased lending to nationalized enterprises and began to carry out their estimated funding.

The naturalization of economic relations, the introduction of non-cash settlements between state-owned enterprises and institutions, as well as the depreciation of money led to a significant reduction and simplification of the functions of the financial system. Under these conditions, the functioning of the People's Bank of the RSFSR, which served mainly budget operations, was inexpedient. Therefore, at the end of 1919, the Bank's branches were reorganized into territorial divisions of financial institutions, and on 19 January 1920, the People's Bank of the RSFSR was abolished.

In the context of the new economic policy in October 1921, the bank was restored under the name of the State Bank of the RSFSR. In 1923, the State Bank of the RSFSR was transformed into the State Bank of the USSR. The State Bank was part of the People's Commissariat of Finance and reported directly to the People's Commissar of Finance.

In November 1921, the State Bank was granted a monopoly right to conduct operations with currency and currency values. The Bank also had to establish the official exchange rate for precious metals and foreign currency, regulating allowed in 1922 private transactions for the sale and purchase of gold, silver, foreign currency, as well as checks and bills issued in foreign currency.

On 11 October 1922, the State Bank gained the right to issue "chervonets" – banknotes into circulation, and the Bank turned into an emission centre.

Since 1922, the establishment of commercial banks began in the country, including sectoral joint-stock banks (special banks) and mutual credit assosiations, which were to carry out short-term or long-term lending to certain sectors of the economy. In 1924, the Committee on the Affairs of Banks was created under the Board of the State Bank, which was supposed to coordinate their activities.

In June 1929, the first Charter of the State Bank was adopted, according to this Charter the Bank was the body regulating money circulation and short-term lending in accordance with the general plan for the development of the national economy of the USSR.

In March 1950, the gold rate of the ruble was established in the amount of 0,222168 g of pure gold.

In December 1949, the second Charter of the State Bank was adopted. In October 1960, the third Charter of the State Bank was adopted, and since 1963, the state labor savings banks were transferred under the supervision of the State Bank. In September 1988, the fourth Charter of the USSR State Bank was approved, in accordance with this Charter it became the main bank of the country, a single issuing centre, organizer of credit and settlement relations in the national economy.

On 13 July 1990, on the basis of the Russian Republican Bank of the State Bank of the USSR, the State Bank of the RSFSR was created with reporting to the Supreme Council of the RSFSR.

On 2 December 1990, the Supreme Council of the RSFSR adopted the Law on the Central Bank of the RSFSR (Bank of Russia), according to this law the Bank of Russia was a legal entity, the main bank of the RSFSR and was reporting to the Supreme Soviet of the RSFSR. The law defined the functions of the bank in organizing of monetary circulation, monetary regulation, foreign economic activity and regulation of joint-stock and cooperative banks.

In June 1991, the Charter of the Central Bank of the RSFSR (Bank of Russia), reporting to the Supreme Soviet of the RSFSR, was approved.

In November 1991, in connection with the formation of the Commonwealth of Independent States and the abolition of USSR structures, the RSFSR Parliament declared the Central Bank of the RSFSR the only state monetary and currency regulation body of the republic in the RSFSR. The Bank was entrusted with the functions of the USSR State Bank for issuing and determining the ruble exchange rate. Before 1 January 1992, the Central Bank of the RSFSR was instructed to take into its full economic management and management all the property of the USSR State Bank.

On 20 December 1991, the State Bank of the USSR was abolished and all its property in the territory of the RSFSR was transferred to the Central Bank of Russia.

The Central Bank of the Russian Federation (Bank of Russia) was established on 13 July 1990. It was accountable to the Supreme Soviet of the RSFSR and was originally called the State Bank of the RSFSR.

Since December 1992, the Bank of Russia has began the process of transferring the functions of the cash execution of the state budget to the newly created Federal Treasury by the Bank of Russia.

In 1992–1995 in order to maintain the stability of the banking system, the Bank of Russia created a system of supervision and inspection of commercial banks, as well as a system of currency regulation and currency control. As an agent of the Ministry of Finance, the Bank of Russia organized the government securities market (GKO) and began to take part in the operation.

The modern Bank of Russia is justly considered to be a body of banking regulation and supervision, since it is the one who performs in aggregate three functions in relation to the banking system and banking activity – permissive, rule-making and regulation by banking regulations. (Chernikova, 2009: 144–145). At the same time, the scientific literature notes that for Russia, with its traditionally formed propensity for centralized state power and the socio-economic realities of development, the coordination forms of banking regulation are also appropriate and relevant, and the Bank of Russia, as the regulator, is the main coordinator there. (Chernikova, 2009: 90–95).

3 Legal regulation of the activities of the Central Bank of Russia in modern times

3.1 Constitutional provisions on the status of the Central Bank of Russia

In accordance with the Russian Constitution, the protection and

the stability of the ruble is the main function of the Central Bank of the Russian Federation, which it performs independently of other government bodies. According to the language of the basic law, the Bank is opposed to other bodies, therefore, it is also a state authority.

Besides, according to clause (g) of Article 71, the issue of money is under the jurisdiction of the Russian Federation. And the Article 73 provides that outside the jurisdiction of the Russian Federation and the powers of the Federation on matters of joint jurisdiction of the Russian Federation and its subjects, the latter have full state power, which suggests that the federal authorities also have full state power on their exclusive competence (Russian Constitution, Article 71). Thus, the decisions on the issue of money, as well as the establishment of a legal framework for a single market; financial, currency, credit regulation; the activities of federal banks should be accepted by the federal government bodies. This fact confirms that the Russian Central Bank should relate to the authorities.

At the same time, the Article 10 of the Russian Constitution stipulates that state power in Russia is exercised on the basis of separation into legislative, executive and judicial, and the Central Bank is not included in any of the specified branches of government. Clause 1 of Article 11 directly states that state power in the country is exercised by the President of the Russian Federation, the Federal Assembly (the Federation Council and the State Duma)–the national parliament, the Government of the Russian Federation, the courts. It should be noted that the federal legislation also lacks a rule on the belonging of the institute of presidency to any branch of government, which causes heated discussions within the country and ambiguous decisions on this matter.

For many years in the scientific and educational literature, the Bank, along with the Accounts Chamber, the Central Election Commission, the Commissioner for Human Rights, the prosecutor's office (and the Investigative Committee separated from it), belonged to authorities that are not part of any branch of the government. At the same time, in foreign countries, the experts note a tendency towards the formation of the fourth branch of government – the control and supervisory one, from similar authorities. Russian Bank exercises banking financial control.

According to the Article 75 of the Russian Constitution, the issue of money in Russia is carried out exclusively by the Central Bank.

The President of the Russian Federation submits to the State Duma (House of Parliament) a candidature for the appointment and dismissal of the Chairman of the Central Bank of Russia (Russian Constitution, clause "d" of Article 83; clause "c" of Article 103).

3.2 Legislative regulation of the activities of the Russian Central Bank

The federal law dated10 July 2002 No. 86-ФЗ "On the Central Bank of the Russian Federation (Bank of Russia)" is currently in force in Russia. The functions and powers provided for by the Constitution of the Russian Federation and the mentioned law are exercised by the Bank of Russia independently of other federal bodies of state power, bodies of state power of subjects of the Russian Federation and bodies of local self-government.

The Bank of Russia is a legal entity. In the Unified State Register of Legal Entities, it is registered in the organizational and legal form of the federal state budgetary institution (extract from the registry – https://www.list-org.com/company/786393). According to Russian civil law, this is a non-profit unitary organization, so making a profit is not the main goal of the Bank. It is created by the sole founder – the state (represented by the authority), and is not the owner of its property, which is transferred to an institution on a limited real right – operational management.

According to the Article 296 of the Civil Code of Russia, an institution, which is secured by the right of operational management, owns and uses it in accordance with the objectives of its activities, the purpose of this

property and dispose of this property with the consent of the owner of this property.

The owner of property has the right to withdraw excess, unused or misused property assigned to the owner by the institution or acquired by him at the expense of funds allocated to him for this by the owner.

The authorized capital and other property of the Bank of Russia are federal property. The Bank of Russia has an authorized capital of 3 billion rubles. It exercises authority for the possession, use and disposal of Bank property, including gold and foreign exchange reserves. Withdrawal and encumbrance of the said property without the consent of the Bank of Russia are not allowed, unless otherwise provided by law.

The state is not responsible for the obligations of the Bank of Russia, and the Bank is not responsible for the obligations of the state, if they have not assumed such obligations or unless otherwise provided by law. The Bank of Russia carries out its expenses from its own revenues.

The objectives of the Bank of Russia are:

- protection and stability of the ruble; development and strengthening of the banking system of the Russian Federation; ensuring the stability and development of the national payment system; development of the financial market of the Russian Federation; ensuring the stability of the financial market of the Russian Federation.

In this regard, the Bank performs the following functions (Central Bank Law, Article 4):

- in cooperation with the Government of Russia, develops and conducts a unified state monetary policy, as well as a policy of development and ensuring the stability of the national financial market; monopolizes the issue of cash and organizes cash circulation; approves the graphic designation of the ruble in the form of a sign; is a lender of last resort for credit institutions, organizes a system for refinancing them; sets the rules for making settlements in the country; supervises and monitors the national payment system; sets the rules for conducting banking operations;
- carries out maintenance of accounts of national budgets of all levels; manages its gold reserves; decides on the state registration of credit

institutions, issues licenses to credit organizations for banking operations, suspends them and revokes them; makes decisions on the state registration of non-state pension funds; supervises the activities of credit institutions and banking groups; regulates the activities of non-credit financial organizations; carries out registration of issues of issued securities and prospectuses of the specified documents, registration of reports on the results of their issues; controls and supervises the compliance of issuers with the requirements of the Russian legislation on joint-stock companies and securities; regulates, controls and supervises corporate relations in joint-stock companies; carries out independently or on behalf of the Government of the Russian Federation all types of banking operations and other transactions necessary to perform the functions of the Bank of Russia; organizes and implements currency regulation and currency control; determines the procedure for effecting settlements with international organizations, foreign states, as well as with legal entities and individuals; approves industry accounting standards for credit institutions, for the Bank itself and for non-credit financial organizations, the chart of accounts for credit and non-credit organizations and the procedure for its application; sets and publishes official exchange rates of foreign currencies against the ruble; takes part in the development of the balance of payments forecast of the Russian Federation; takes part in the development of the methodology for compiling the financial account of Russia in the system of national accounts and organizes the compilation of the state financial account; organizes the compilation of the balance of payments of Russia, the international investment position of the state, statistics on foreign trade in services, external public debt, international reserves of Russia, direct investments in the Russian Federation and direct investments from it abroad; analyses and forecasts the state of the national economy, publishes relevant materials and statistical data; makes payments to the Bank of Russia on deposits of individuals in banks recognized as bankrupt and not participating in the system of compulsory deposit insurance in banks; is a depository of the International Monetary Fund funds in the currency of the Russian Federation; it carries out operations and transactions stipulated by the Articles of Agreement of the International Monetary Fund and agreements

with the International Monetary Fund foundation; monitors compliance with the requirements of the legislation of the Russian Federation on countering the unlawful use of insider information and market manipulation; protects the rights and legitimate interests of shareholders and investors in financial markets, insurers, insured persons and beneficiaries recognized as such in accordance with insurance legislation, as well as insured persons for mandatory pension insurance, depositors and participants of non-state pension fund for non-state pension provision; organizes the provision of services for the transmission of electronic messages on financial transactions and other functions.

The Bank of Russia is accountable to the State Duma of the Federal Assembly of the Russian Federation (Article 5).

According to the law, the State Duma also appoints and dismisses members of the Board of Directors of the Bank on the proposal of its Chairman, agreed with the President of Russia; considers the annual report of the Bank and makes decisions on it; decides on the audit by the Accounts Chamber of the financial and economic activities of the Bank and its structural divisions and institutions; holds parliamentary hearings on the activities of the Bank of Russia with the participation of its representatives; hears reports of the Chairman of the Bank on the activities of this organization (when presenting the annual report and the main directions of the unified state monetary policy).

The Central Bank issues regulations on questions within its competence (the Law on the Central Bank, Article 7), which is usually the power of the state authorities (Chebykina, 2006).

The collegiate body of the Bank is the National Financial Council. The number of council members is 12, of which two are sent by the Council of Federation of the Federal Assembly (upper chamber of the national parliament) from among its members, three by the State Duma (lower chamber of parliament) from among its deputies, three by the President, three by the Government. The National Financial Council also includes the Chairman of the Bank. Council members (with the exception of the Chairman of the

Bank) do not work at the Bank on an ongoing basis and do not receive payment for this activity.

The Chairman of the National Financial Council is elected by its members from among their number by a majority vote.

Members of the Board of Directors, the executive body of the Bank, work on a permanent basis there. This Council consists of the Chairman and 14 members who are appointed by the State Duma for a term of five years on the proposal of the Chairman of the Bank, agreed with the President.

The Bank participates in the development of the economic policy of the Russian Government. The Chairman or one of his deputies participates in meetings of the Government, and can also participate in meetings of the State Duma when considering draft laws relating to economic, financial, credit and banking issues.

The Minister of Finance and the Minister of Economic Development of Russia or one representative from the indicated ministries participate in meetings of the Board of Directors with an advisory vote.

The Bank and the Government inform each other about the proposed actions of national importance, coordinate their policies, conduct regular mutual consultations.

The Bank of Russia advises the Ministry of Finance of the Russian Federation on the schedule for issuing government securities and repaying government debt.

The Bank is not entitled to provide loans to the Government of Russia to finance the deficit of the federal budget, the budgets of the subjects of the Federation, or to buy government securities upon their initial offering, except when it is required by law.

4 Conclusion

In conclusion, we can infer that in Russia the legal status of the Central Bank is not defined. According to the Constitution, the functions of this institution are considered by analogy with the powers of the authorities. Besides, the Bank adopts obligatory regulations, which are typical of the

state authorities. The Ministry of Finance of Russia in its letter (the act is not normative) in 2019 directly listed the Central Bank among the federal executive bodies. But the according to the law it does not include some special features. The legal form of the budget institution in which the Bank is registered does not correspond to the form of the Russian authorities. Its sole founder is the state, in whose property continues the property transferred to them by the Bank. Thus, this is a different public law state organization with a special status, the similarity of which we cannot find at the national level. Based on the analysis of foreign practice in the matter under inquiry, one can conclude that a similar situation has developed in most other states.

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The Influence of Changes in the Legislation on the Russian Audit Market

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Abstract

The paper deals with the correlation between the changes in statutory regulation of audit activities (one of the components of the financial law), and the development of audit business being a part of financial market infrastructure. The authors develop a hypothesis that audit market is strongly influenced by the respective laws and regulations on audit activities. This hypothesis is confirmed by the behavior of the key Russian audit market indicators in 2011–2017. In their research the authors use the methods of analysis, synthesis, historical and systematic approach, as well as the methods of generalization, specification, classification and interpretation.

Keywords: Audit; Financial Market; Law; Audit Organizations.

JEL Classification: K39; M42.

1 Introduction

According to the definition given by the Central Bank of Russia, financial market is the system of economic and legal relations that imply financial instruments circulation and the use of money as a store of value and a means of payment, as well as a legal and cultural business environment for financial market participants. The result of activities in the financial market is efficient allocation of financial resources and risks, as well as formation

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of fair prices for financial assets (Central Bank of Russia, 2018: 4). Financial market participants are creditors, investors and investment objects, while its infrastructure is formed by depositories, clearing organizations, rating agencies, credit bureaus, actuaries, auditors and other parties.

Auditors take an active part in the creation of financial market infrastructure, and their activities depend largely on the regulatory environment.

In this article the authors aim to show the influence of major changes in laws and regulations providing for audit activities within the respective jurisdiction on the dynamics of audit market. The target of this paper is to study the statutory basis of audit activities in the Russian Federation, as well as the Russian audit market.

To achieve this target, the authors use the methods of analysis, synthesis, historical and systematic approach, as well as the methods of generalization, specification, classification and interpretation.

The topic of the Russian audit market dynamics has been studied by K. K. Arabyan (Arabyan, 2016), I. N. Bogataya (Bogataya, 2017), R. P. Bulyga (Bulyga, 2016), S. V. Cheremisina (Cheremisina, 2014), E. I. Erokhina, V. S. Karagod, N. A. Golubeva (Erokhina, Karagod, Golubeva, 2017), V. P. Goreglyad (Goreglyad, 2017), Y. N. Guzov (Guzov, 2016 (1), (2)), N. A. Loseva (Loseva, 2016), M. V. Melnik (Melnik, 2018), U. Y. Roshchektayeva (Roshchektayeva, 2017), A. D. Sheremet (Sheremet, 2017), A. V. Turbanov (Turbanov, Lisovskaya, 2015; Turbanov, 2017; Turbanov, 2018), I. A. Lisovskaya (Turbanov, Lisovskaya, 2015) and others. In their works these authors discuss the combination of factors that influence the basic market characteristics. In this paper we are going to consider the impact of one of the major factors – the changes in the Russian statutory basis of audit activities.

2 The History of Development and the Modern State of the System of Audit Activities Statutory Regulation

It can be said that the development of the Russian system of audit activities statutory regulation started on 2 December 1990, when the Law on Banks

and Banking Activities in RSFSR # 395-1 was adopted (Law on Banks and Banking Activities in RSFSR, Art. 17, 24, 43, 45). It was mentioned in Article 45 of this law that banking activities are subject to annual audit by competent organizations. On 6 February 1991, the Regulation on Audit Activities in RSFSR Banking System was approved by the Central Bank of Russia (Regulation on Audit Activities in RSFSR Banking System).

The first legal act regulating audit in the Russian Federation regardless of the industry to which the audited entity belonged was the Decree of the President # 2263 of 20 December 1993 On Audit Activities in the Russian Federation. This decree provided for the temporary rules for audit activities in the Russian Federation (Decree On Audit Activities in the Russian Federation, Art. 1).

The current legislation on audit activities can be classified as follows:

- Federal level;
- professional self-regulation level.

The Federal level includes:

- the Federal law On Audit Activities providing for the legal basis of audit activities regulation in the Russian Federation (Federal law On Audit Activities, Art. 2);
- other Federal laws providing for particular aspects of audit activities, such as the Federal law On Self-Regulatory Organizations (Federal law On Self-Regulatory Organizations), the Federal law On Countermeasures to Combat Legalization (Laundering) of Illegally Obtained Proceeds and Financing of Terrorism (Federal law On Countermeasures to Combat Legalization (Laundering) of Illegally Obtained Proceeds and Financing of Terrorism, Art. 7.1) and others;
- by-laws regulating at the Federal level certain aspects of audit activities, such as: the creation of a Council for Audit Activities and a Unified Certification Commission, award of auditor's qualification certificates etc.;
- standards of audit activities. In the Russian Federation audit activities are performed on the basis of international audit standards and other documents issued by the International Federation of Accountants (IFAC).

The level of professional self-regulation is represented by the documents adopted by each self-regulatory auditors' organization, including:

- the approved code of professional conduct;
- the approved rules of auditors' and audit organizations' independence;
- the standards of audit activities for self-regulatory auditors' organizations;
- the rules for organization and external control of the quality of work of the members of a self-regulatory auditors' organization etc.

In our opinion, in the past few years, the most significant changes in audit activities statutory regulation have been:

- the changes in the order of auditor's qualification examination organization in January 2011;
- progressive broadening of the range of business units whose financial statements are subject to mandatory audit as per the Federal law *On Audit Activities*, and other Federal laws;
- Russian auditors' transition to international standards.

Let us see the impact of these changes on the Russian market of audit services.

In accordance with part 2, article 15 of the Federal law On audit activities, the Ministry of Finance of the Russian Federation, being the Federal-level supervisor of Russian audit, also analyzes the state of the Russian audit market. Every year the results of this analysis are published on the website of the Ministry of Finance in the form of analytical reports issued separately for audit organizations and auditors (Ministry of Finance of the Russian Federation, 2011–2017). These analytical reports are formed on the basis of the reference copy of the Register of Auditors and Audit Organizations provided by the Ministry of Finance, and the Form of Federal Statistical Monitoring #2 – audit (Information on Audit Activities). The data for this form are collected and processed in the information management system of the Ministry of Finance.

When discussing the peculiarities of the Russian audit market, we are going to rely on the reports on audit organizations prepared by the Ministry of Finance in 2011–2017.

3 The Influence of the Changes in the Order of Auditor's Examination Organization on the Number of Russian Auditors

An auditor's qualification certificate is the official proof of the auditor's qualification. Due to the specific character of the activities of the entities belonging to different economic sectors, since December 2002 till October 2009, the Ministry of Finance of the Russian Federation issued the following types of certificates:

- in the sphere of exchanges, non-budgetary funds and institutional investors audit;
- in the sphere of insurance companies and mutual insurance associations audit;
- in the sphere of credit institutions, bank groups and bank holdings audit;
- in the sphere of general audit (audit of entities not listed in (1)–(3)).

Since 1 November 2009 till 31 December 2010, however, the number of certificates was reduced to two:

- in the sphere of credit institutions, bank groups and bank holdings audit (bank audit);
- in the sphere of financial audit of other economic entities.

This innovation was logical, as the differences in the accounting and financial reporting procedures existing in all the economic sectors, except for credit institutions, bank groups and bank holdings, are not so significant.

Since 1 January 2011, there exists only one unified form of a qualification certificate that does not specify the economic sector.

There is no formal requirement for those auditors whose certificates were issued before 1 January 2011 to retake the examination, but their practice is subject to a number of restrictions. Such auditors have a right to perform audit activities provided for by the certificate they own, but cannot participate in mandatory audit of:

- entities issuing securities accepted for on-exchange trading;
- other credit institutions and insurance companies;
- private pension funds;
- entities with no less than 25 % of state-owned assets in their registered capital;

- state-owned corporations;
- state-owned companies;
- pubic law companies;
- financial statements included in the securities prospectus and consolidated financial statements.

As a result of these restrictions, auditors had to spend time and money on additional courses and examinations, although the knowledge they obtained at such courses was of little practical use. Audit organizations, in their turn, incurred expenditures associated with retraining of their employees.

Due to multiple refusals to take qualification examination in its new format, the number of auditors and audit organizations stopped growing in 2012 and has been decreasing since then (see Table 1).

Table 1: The number of auditors and audit organizations in the Russian Federation (thousand)

Categories	As of 1 January 2011	As of 1 January 2012	As of 1 January 2013	As of 1 January 2014	As of 1 January 2015	As of 31 December 2015	As of 31 December 2016	As of 31 December 2017
1. Have the right to perform audit activities – total	6.1	6.2	5.7	5.5	5.3	5.1	5.0	4.8
including:								
audit organizations	5.2	5.2	4.8	4.7	4.5	4.4	4.4	4.2
individual auditors	0.9	1.0	0.9	0.8	0.8	0.7	0.6	0.6
2. Auditors – total	26.3	26.8	24.1	23.0	22.2	21.5	19.6	19.6
including those having passed the qualification examination for the unified certificate	X	1.1	3.2	3.2	3.4	3.5	3.6	4.0

Source: Ministry of Finance

Note: in 2015 the reporting date for the formation of statistical key figures describing the number of audit organizations and auditors was shifted from 1 January to 31 December of each year.

By the end of 2018 the share of the auditors having a unified qualification certificate was just 20 % of the total number of auditors.

4 The Influence of the Changes in the List of Cases Subject to Mandatory Audit in the Russian Audit Market

Mandatory audit of the annual financial statements is performed in the cases provided for by Article 5 of the Federal law *On audit activities*, as well as by other Federal laws. The list of such cases is being extended gradually.

For example, since 2 December 2014, the financial statements of all the Russian joint-stock companies are subject to mandatory audit. Before that date this rule applied only to "open" (or "public", if we use the modern term) joint-stock companies. Since 14 July 2015, the financial statements of self-regulatory organizations acting in the financial market are also subject to mandatory audit. Since 2 October 2016, the same rule applies to the financial statements of public law companies, and since 2018, – to the financial statements of associations of tour operators engaged in international tourism.

The statutory extension of the list of entities whose financial statements are subject to mandatory audit leads to the growth of the share of compulsory audit as against other types of audit (see Table 2).

Table 2: Reasons for performing audit in the Russian Federation (%)

Reasons for performing audit	Share of the total number of audits					
	2012	2013	2014	2015	2016	2017
1. Number of auditors' reports given as a result of mandatory audit	81,5	83,3	85,3	88,7	90,6	91,3
2. Number of auditors' reports given as a result of voluntary audit	18,5	16,7	14,7	11,3	9,4	8,7

Source: Ministry of Finance

Before 2016, this had no effect on the decrease of the share of income from audit in the total revenue gained by Russian audit organizations (Table 3). In 2017, for the first time in three years, this share inched up (from 48,9 % to 49,6 % of the total revenue).

Table 3: Revenue structure of Russian audit organizations

Index	2014	2015	2016	2017
1. Share of income from audit in the total revenue per year	51,0	49,2	48,7	49,6
2. Share of income from audit related services in the total revenue per year	5,2	4,0	2,7	5,1
3. Share of income from other types of services in the total revenue per year	43,8	46,8	48,6	45,3

Source: Ministry of Finance

Note: The revenue structure of Russian audit organizations was first shown in the analytical report of the Ministry of Finance of the Russian Federation named *Basic Indices of Audit Market in the Russian Federation in 2014*.

In 2012–2017 the statutory extension of the list of entities subject to mandatory audit led to the growth of the number of clients of audit organizations requesting audit services from 70 044 to 78 087 (table 4).

Table 4: The number of clients of audit organizations whose financial statements have gone through auditing procedures

Year	Russia – total	Moscow	St. Petersburg	Other regions
2012	70 044	26 981	6 583	36 480
2013	68 380	26 773	6 271	35 336
2014	67 857	27 810	5 963	34 084
2015	71 841	27 437	6 419	37 985
2016	74 537	27 299	6 586	40 652
2017	78 087	28 623	6 687	42 777

Source: Ministry of Finance

5 The Influence of the Transition to International Standards on Audit in Russia

In compliance with the orders of the Ministry of Finance of the Russian Federation of 24 October 2016 No. 192n, and of 9 November 2016 No. 207n *On the Introduction of International Audit Standards in the Territory of the Russian Federation*, since 2017, Russian auditors have to work in accordance with the international audit standards and other documents standardizing their professional services, which have been issued by IFAC (Order On the Introduction of International Audit Standards in the Territory of the Russian Federation # 192n, Art. 1; No. 207n, Art. 1).

This transition was predetermined by the following factors:

- the absence of national peculiarities of audit services provision;
- constant delays in the adjustment of Russian audit standards to the international standards. For instance, in the beginning of 2012 only 18 out of 40 Russian national audit standards complied with the international standards. The main differences were associated with Clarity project by IFAC, which was completed in February 2009. In the course of its implementation, all the existing international audit standards were edited and restructured. Eight national standards have been adopted since the project was implemented in the Russian Federation;
- trade relations between the Russian Federation and the countries that use international audit standards and other related documents developed by IFAC.

The transition to international audit standards was an important step that has had significant consequences for all the parties engaged, including auditors, entities under audit (audit clients), all the parties having access to financial statements, parties that are involved in the Government control of audit activities in the Russian Federation, parties that are involved in professional self-regulation of audit activities in the Russian Federation, and Russian Federation itself as a participant of international relations.

To cope with it, Russian auditors had to update the guidelines for audit services provision and to upgrade their qualification.

When the transition to international standards was completed, the parties having access to financial statements, including the audited entities, got sure that in the course of audit a universally recognized procedure was used, and that the results are presented in a universal format that is familiar to stakeholders from different countries.

As IFAC possesses the rights for the Russian translation of the texts of international standards, it is supposed to get royalties for the use of such translated versions. The obligation to pay the royalties is borne by the State.

The function of external control of the quality of work of audit organizations and sole auditors is performed by self-regulatory auditors' organizations. The function of external control of the quality of work of audit organizations engaged in the financial audit of public interest entities is performed by self-regulatory auditors' organizations, as well as by the Federal Treasury.

As per Article 22 of the law *On Audit Activities*, the state control (supervision) of self-regulatory auditors' organizations is performed by the Ministry of Finance of the Russian Federation.

For the Ministry of Finance, the Federal Treasury and self-regulatory auditors' organizations the transition to the international audit standards has entailed the need to revise the programs of external audit.

The use of international standards has made the procedure of audit in Russia universal and recognized by more than 110 jurisdictions all over the world. The introduction of international audit standards was an important step towards the strengthening of economic and legal bonds between countries.

6 Russian Market Peculiarities to be Considered in case of Changes in the Legislation

Let us consider the structure of the Russian audit market which remained quite stable from 2012 to 2017 (see Table 5).

Table 5: Distribution of audit organizations by the scope of activities (%)

Year	Share of the total number of audit organizations	Share of the total scope of the services provided	Share of the total number of clients whose financial statement were audited
Small			
2012	90,0	24,2	62,3
2013	89,4	23,4	60,7
2014	91,1	23,7	62,4
2015	91,6	23,3	64,8
2016	90,8	23,0	63,1
2017	90,8	22,7	63,7
Medium-sized			
2012	8,8	16,8	23,1
2013	9,4	15,7	23,2
2014	7,7	13,3	20,6
2015	7,2	11,7	18,8
2016	7,9	11,7	20,3
2017	7,9	12,1	19,7
Large-scale			
2012	1,2	59,0	14,5
2013	1,2	60,8	16,1
2014	1,2	63,1	17,0
2015	1,2	65,0	16,4
2016	1,3	65,1	16,6
2017	1,3	65,2	16,6

Source: Ministry of Finance

Note: small audit organizations are organizations with less than 15 employees, medium-sized organizations are those with 15–50 employees, and large-scale are those with more than 50 employees.

One of the peculiarities of the Russian market is the prevalence of small-scale audit organizations. In 2012–2017 they accounted for 89,4–96,1 % of the total number of audit organizations. During this period small-scale audit organizations performed 60,7–64,8 % of audits, while their share

in the total amount of services provided was 22,7–23,7 %. It is evident that the cost of their services was the lowest among all the three categories of audit organizations.

Most of the profit from audit activities was gained by large-scale enterprises that accounted for 59–65,2 % of the total annual earnings of audit organizations. However, large-scale enterprises performed fewer audits that the other two categories of audit organizations, 17 % on average. Their share in the total number of audit organizations was only about 1,2–1,3 %

During this period there were no significant changes in the client structure of Russian audit organizations: 63,3–66,3 % of the clients were the entities earning less than 400 m rubles per year, 28–30,8 % of the clients earned from 400 m to 4 b rubles per year, while 4,7–6 % earned more than 4 b rubles per year (see Table 6).

Table 6: Clients of Russian audit organizations whose financial statements were analyzed, by revenue

Annual revenue	Share of the total number of clients, %					
	2012	2013	2014	2015	2016	2017
1. Less than 400 m rubles	65,8	65,1	63,3	65,0	66,2	66,3
2. 400 m-1 b rubles	18,9	18,7	19,2	18,4	16,8	16,5
3. 1–2 b rubles	6,9	6,9	7,4	7,3	7,2	7,1
4. 2–4 b rubles	3,7	4,1	4,2	4,0	4,0	4,1
5. More than 4b rubles	4,7	5,2	5,9	5,4	5,8	6,0

Source: Ministry of Finance

The stability of clients' and auditors' structure was, to a large extent, caused by the audit market stratification. Traditionally, the entities that are at the top of the market have to have their auditor's opinion signed by a particular person. Smaller enterprises do not have such restrictions.

When changes are introduced into audit legislation, it must be remembered that most of the audit organizations and their clients are small and medium-sized enterprises (see Table 5). On the other hand, most of the audited enterprises could not elect not to go through audit procedures because of the legal requirements (see Table 2).

7 Conclusion

In this article we have empirically proved the hypothesis about the influence of the changes in laws and regulations providing for audit activities on the audit market behavior. The subject of this study is the statutory basis of audit activities in the Russian Federation, as well as the Russian audit market.

In our opinion, in the past few years, the most significant changes in audit activities statutory regulation have been:

- the changes in the order of auditor's qualification examination organization in January 2011;
- progressive broadening of the range of business units whose financial statements are subject to mandatory audit as per the Federal law *On Audit Activities*, and other Federal laws;
- Russian auditors' transition to international standards.

These changes have had the following impact on the Russian audit market:

- due to multiple refusals to take qualification examination in its new format provided for by the Federal law *On Audit Activities*, which was introduced in 2011, the number of auditors and audit organizations stopped growing in 2012. Since then the number of entities involved in audit activities has gone down from 5,7 thousand in the end of 2013 to 4,8 thousand in the end of 2017;
- the statutory extension of the list of entities whose financial statements are subject to mandatory audit has resulted in continuous growth of mandatory audit share in the total number of audits: from 81,5 % in 2012 to 91,3 % in 2017. Till 2016 this did not have any impact on the general tendency for the reduction of the share of audit in the total revenue of Russian audit organizations. In 2017 for the first time in four years this figure inched up from 48,9 % to 49,6 %. At the same time, in 2012–2017, these changes in the legislation led to the increase in the number of clients of audit organizations requesting audit services from 70,044 to 78,087;
- the transition to international audit standards has had significant consequences for all the parties engaged, including auditors, entities under audit, all the parties having access to financial statements,

parties that are involved in the Government control of audit activities, parties that are involved in professional self-regulation of audit activities, and Russian Federation itself as a participant of international relations.

To cope with this challenge, Russian auditors had to update the guidelines for audit services provision and to upgrade their qualification.

As a result, the parties having access to financial statements were convinced that in the course of audit a universally recognized procedure was used.

For the Ministry of Finance, the Federal Treasury and self-regulatory auditors' organizations the transition to the international audit standards has entailed the need to revise the programs of external control of auditors' performance quality.

The introduction of international audit standards was another step towards the strengthening of economic and legal bonds between countries.

When changes are introduced into audit legislation, it must be remembered that most of the audit organizations and their clients are small and medium-sized enterprises, while most of the audited enterprises cannot avoid going through audit procedures because of the existing legal requirements

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Financing of the Agro-Industrial Complex of Russia

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Abstract

The article systematizes the ways of financing of the agro-industrial complex of modern Russia and their legal regulation. Centralized budget financing of agriculture is now in the past. Agricultural organizations conduct activities on the basis of self-financing; in addition, they search for other development options by attracting investors and funds. However, agriculture and the agro-industrial complex are supported in the form of subsidies under the terms and conditions of co-financing by the subjects of the Russian Federation. There are several priority directions of support of agricultural industries. The procedure and objectives of state support are established in the State Program for Development of Agriculture and Regulation of Agricultural Commodities Markets[2]. Russia's accession to the WTO required a reduction of government intervention in market relations. One of the ways to develop the state funding of agriculture is to shift from process form of financing to project financing.

Keywords: Financing; Budget Financing; Self-Financing; Subsidies; Grants; Investments; Lending; Agriculture; Project Method.

JEL Classification: K2.

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2 Постановление Правительства РФ от 14. 7. 2012 N 717 (ред. от 30. 11. 2018) "О Государственной программе развития сельского хозяйства и регулирования рынков сельскохозяйственной продукции, сырья и продовольствия на 2013–2020 годы" (Order of the Government of the Russian Federation of 14. 7. 2012 N 717(edited on 30. 11. 2018) "About the State program of development of agriculture and regulation of the markets of agricultural production, raw materials and the food for 2013-2020") // Corpus of Legislative Acts of the Russian Federation, 6. 8. 2012, N 32, p. 4549.

1 Introduction

The article aims to identify current trends in financing of the agro-industrial complex of Russia and their legal registration. The analysis has been performed using general and special scientific methods (dialectical, historical and systemic approaches, analysis and synthesis, comparative legal study, content analysis of normative documents). The idea of changing the paradigm of budget financing to self-financing was used as a hypothesis, along with the associated change in the following principles of financing: the move from centralized planning to strategic planning and program management, participation of subjects of the Russian Federation in financing, identification of priority directions of agricultural support, contractual relations in the field of public finance, and the replacement of process financing by project financing. This topic is related with international trade as well. According to Costinot et al. (2015), the first one, at the intersection of international trade and public finance, is related to the classical problem of optimum taxation in an open economy.

Very few legal scholars have been interested in the topic of financing of the agro-industrial complex of Russia. Scientists studying financial law have overlooked the specific features of agriculture, while agrarian and legal science has left it up to specialists in financial law to research the problems of financial support. The main body of research has been focused on selected issues of financing: financial recovery of insolvent agricultural producers (Matigina, 2004), credit relations in agriculture (Akmanov, 1999; Popova, 2009), legal regulation of financial relations of agricultural commercial organizations (Hannanova & Balashov, 2008), or activities (Amineva, 2005), legal regulation of settlements in agricultural production (Nedorezkov, 2000); legal provision of banking services to agricultural producers (Hannanova, 2001).

It is mostly the economists who devote their research to the problems of the agro-industrial complex financing, often focusing on one of the regions in Russia. At the same time, it is impossible to highlight any studies that would deal with the holistic comprehension of agriculture financing.

2 Budget financing of the agro-industrial complex of Russia

In Russia, before Mikhail Gorbachev's rise to power and the onset of restructuring and reformation, the agricultural sector, like others, was financed centrally from the state budget according to the state plan. In 1991, the budget system was re-established on different democratic principles (Boltinova, 2015: 74). Unregulated market economy gave rise to hyperinflation and price disparity, which in turn led to the insolvency of most agricultural enterprises, food shortages, and threats to national sovereignty. Russian economy failed to be modernized and was completely destroyed. It became clear that unregulated wild market is not the best option for a big country.

The situation required urgent measures in agriculture financing, and in the period from 1990 to the present different ways of supporting agricultural producers have been developed: financial recovery of agricultural enterprises, preferential loans, leasing support, insurance support, and some others.

Currently, Russia has revived the planning institute, but on an entirely new foundation. Strategic planning is founded on a situational basis with regard to future periods, to what is desirable to achieve, as opposed to planning based on the development prospects for the current situation.

Now the economic situation has slightly improved. The Budget Code of the Russian Federation[3] (hereinafter – BC RF) provides for the following types of budget financing: non-earmarked general grants (inter-budgetary transfers on a non-reimbursable and irrevocable basis without establishing the directions of their use), subventions (inter-budgetary transfers for financing expenditure obligations in the course of exercising delegated authority), and subsidies. Subsidies may be granted to legal entities and individuals. Subsidies are provided as per agreement between the Russian Federation (the authorized body within the sphere of agriculture is the Ministry of Agriculture of the Russian Federation) and a federal subject, i.e. a constituent entity

3 Бюджетный кодекс Российской Федерации (Budget Code of the Russian Federation) from 31. 7. 1998 N 145-FZ (ed. 3. 8. 2018) // Corpus of Legislative Acts of the Russian Federation. 3. 8. 1998, no. 31, Art. 3823.

of the Russian Federation (or between a federal subject and a municipality), as well as between a federal subject (municipality) and a juridical or a natural person. A subsidy for a subject of the Russian Federation (municipality) is, as a rule, provided on condition of co-financing. In the relations between the budget of the Russian Federation (municipality) and a juridical (or a natural) person, there is often an additional subject – a private investor, often called an industrial partner in such agreements. In some cases, subsidies are provided in the form of grants for realizing a socially useful project, such as for opening a museum or a library in a village. In this case, a grant is comparable to a donation agreement, viewed as state participation in charitable activities. But sometimes subsidies that are provided to peasant farming (farms) as to small businesses subjects in order to create or develop a business, or to change the profile of business because of the threat of spreading African swine fever, are also called grants.

Thus, there is no clear conception of financing of the expenditures by the state in the form of subsidies, and the legal regime of these public contracts remains uncertain. In addition, ambiguity in the methodology of accounting for earmarked federal funding also significantly complicates the lives of economic entities (Sergeeva, 2015: 147).

Budget financing of the agro-industrial complex is realized by way of state support. State support for agricultural producers is provided within the framework of the Federal Law of 29. 12. 2006 N 264-FZ "On development of agriculture"[4]. This law highlights the main directions of state support of agricultural development. The State Program for Development of Agriculture and Regulation of Agricultural Commodities Markets provides specifics of this support.

Federal funds, as allocated by the Federal Law on the federal budget for the next fiscal year to support the agricultural development, are granted to the budgets of federal subjects as subsidies in a procedural order established by the Government of the Russian Federation.

4 Федеральный закон "О развитии сельского хозяйства" (Federal law from 29. 12. 2006 no. 264-FZ (ed. 29. 7. 2018) "On the development of agriculture") / / Corpus of Legislative Acts of the Russian Federation, 1. 1. 2007, no. 1 (part 1), Art. 27.

Support of the agro-industrial complex is provided in the form of several types of subsidies: "single", per hectare, for development of dairy farming, agricultural land reclamation, grant support for rural residents, purchase of housing for rural specialists, road construction, crediting.

The "single" subsidy is transferred to the budgets of the federal subjects in one payment. Subjects of the Russian Federation choose sectors and the extent of the support independently. Budget allocations can be redistributed between the sectors within a "single" subsidy, taking into account the need to achieve the targets. Thus, it is expected that such mechanism will contribute to increasing the autonomy of federal subjects in choosing the methods for achieving their objectives; it aims for efficiency and gives hope for effective use of budgetary funds, as well as for delivery of budgetary allocations, fully and in a timely manner, to the final recipients – agricultural producers.

In addition to this form of subsidies, another option of support is the provision of decoupled support intended for partial reimbursement of the cost of completing a range of agrotechnological works that increase crop production. The decoupled subsidy for agricultural producers is not linked to the current indicators of their production, the results of increased production volumes, etc. It is also called a per hectare subsidy, as it is provided at rates calculated per hectare of cultivated area. The per hectare subsidy is intended for crop production, including production of seed potatoes, seeds of open ground vegetable crops, corn seeds, sunflower seeds, sugar beet seeds, flax, industrial hemp and open ground vegetables, as well as for partially subsidizing the cost of carrying out agrotechnological works, facilitating preparation for sowing and harvesting campaigns, stimulating investment in improving yields and soil quality. This subsidy can also be obtained through the regional agency of the agro-industrial complex.

Decoupled subsidy is similar to "single" subsidy only at first glance. However, while a single subsidy stimulates the expansion of acreage, decoupled support is aimed at land conservation, including improvement of soil quality and fertility, and ecological safety of agricultural production. Decoupled subsidy is calculated according to profit indicators in crop production, profitability from sales of crop production, soil fertility indicator, wherein

the highest indicator score is assigned the lowest rank value. "Decoupled support" is drawn from the practice of Western countries (Polulakh et al, 2018: 76).

3 Lending as the main form of financing of the agro-industrial complex of Russia

However, subsidies for the activities of agricultural organizations can only be an additional source of financing of the agro-industrial complex. Yet, features of agriculture are specific in such way that the uneven flow of income and the gap between bearing the costs and receiving the revenue necessitate the search for borrowed investment funds. At the same time, the risky nature of agriculture, its dependence on climate, weather and other factors makes agriculture unattractive for banks. Nevertheless, lending is one of the main sources of financing both for innovations in crop production (Babaeva, 2018) and in general financing of crop and animal husbandry. In this regard, it follows that lending to agricultural producers also requires state support. The legal institution of lending to agricultural producers has changed its conception throughout the development of modern Russia.

Until 1 January 2017, the support for lending to agricultural producers was implemented in the form of subsidizing the interest rate on loans received by the producers in banks; loans were provided on general terms. Agricultural producers were not satisfied with this procedure, as the subsidy might have not even been received while the loan agreement was already concluded, and the fulfillment of loan conditions at high rates became an unbearable burden for an agricultural producer.

From 1 January 2017, subsidies are provided directly to lending institutions which have been selected as authorized bodies by the Ministry of Agriculture. The interest rate on preferential loans cannot exceed 5 %. Reimbursement of the loss of profit to a lending institution comes directly from the federal budget at the key interest rate of the Bank of Russia. There can be both short-term and investment loans. Loans are issued for a period of 2 to 15 years. Depending on the intended purposes, agricultural organizations, as well as peasant farmers and citizens with private subsidiary farms,

can act as borrowers. Lists of intended purposes of preferential loans are regulated by the Ministry of Agriculture. A list of precise purposes eligible for a preferential loan is supplied in the above-mentioned document of the Ministry of Agriculture of Russia. The objectives of preferential lending are the development of crop production and animal husbandry, and food and processing industries.

Preferential investment loans for the purpose of construction and (or) reconstruction of processing enterprises can be granted provided that these enterprises process at least 70 % of Russian agricultural raw materials.

Loans granted between 2006 and 31 December 2016, which have not yet been refunded are also subject to subsidies, but on the previously existing terms.

As we see, for an agricultural producer or a rural resident (even more so) who is not a specialist neither in budgetary law nor in the law as a whole, understanding rights and opportunities for obtaining state support is not easy. There is no single definition for measures of state support of agriculture (Gleba, 2018: 17), and no single list of such measures. Therefore, it is crucial to develop another area of support – informing the public about the support measures available to them. These objectives can be achieved through the use of specialized information systems; apart from that, a Federal Government Budget Institution, which is called Federal Agency of State Support of Agriculture and administered by the Ministry of Agriculture, has been established to fulfill the state assignment.

4 New forms of financing of the agro-industrial complex of Russia

The state support measures to some extent include purchasing and commodity interventions (Popova, 2016: 95), when the state acts as a buyer or seller in the agricultural commodity market in strictly defined cases in order to prevent product shortages and preserve food security of the state.

Although support is also provided as pertaining to insurance, this does not mean that the state insures agricultural products at its own expense. The law

outlines limitations on both the objects of agricultural insurance and agricultural risks under which the state support is given.

Also, in order to equalize the profitability of agricultural producers, there is a mechanism of state support which establishes preferential tariffs for the transportation of certain types of agricultural products for export. Thus, financing can be holistic and include the institutional framework and budgetary funding itself. For example, in order to increase the availability of agricultural machinery, producers who sell such equipment at a discount are granted subsidies from the federal budget (the funds are administered by the Ministry of Agriculture of Russia, although the decision is made by another agency – the Ministry of Industry and Trade). In addition, JSC "Rosagroleasing" was created, the main purpose of which was supposed to be leasing the activities within the domain of agricultural machinery and equipment. The authorized capital of JSC "Rosagroleasing" was formed at the expense of budgetary funds, and subsidies are provided not directly to agricultural producers, but to manufacturers of agricultural machinery (Babaeva et al., 2017: 7; Zemlyakova, 2004: 22). Another example of such institutional structures can be JSC "Rosselkhozbank", which was created with the objective of facilitating lending to agricultural producers.

However, the effectiveness of such institutions and the exclusion of corrupt factors in their functioning are questionable.

Moreover, it should be noted that the policy of liquidating state enterprises is being implemented (Popova, 2017: 126). At the core of reducing the number of state-owned enterprises, the operation of which is based on the allocation of authorized fund from the federal budget, lies possible distortion of the market equilibrium, while the same influence of government corporations is not taken into account. It should also be mentioned that public organizations (both state-owned enterprises and joint-stock companies with a share of government funds in their capital) are not under any obligation to disclose information about their benefactors, which also can potentially increase the propensity for corruption in this area.

In general, there is a constant search for interaction between society and the state, economy and law, for the best results, sustainable development, the most efficient ways of financing. One of these modern methods

of financing is a public-private partnership (Shokhin, 2018: 4; Belitskaya, 2017: 42) that aims to attract investments in the Russian economy and improve the quality of goods and services, the organization and provision of which to consumers is a matter of management by public authorities and local government bodies. Funding on a parity basis is also provided in the field of agriculture. Objects of public-private (municipal-private) partnership agreements can be agricultural reclamation systems and their engineering infrastructure objects, with the exception of state reclamation systems; objects of production, primary and (or) subsequent (industrial) processing, storage of agricultural products according to the criteria established by the Government of Russia, and objects of hunting infrastructure.

In recent years, self-financing through independent entrepreneurship (agricultural organizations, peasant farms), attraction of private investments and cooperation has taken priority over budgetary financing in the agro-industrial complex. "*Effective functioning of expanded reproduction processes is possible only within financial and credit policy that involves interaction of state and non-state financing sources of the complex*" (Gorokhov, 2014: 42). Thus, the system of financing of the agro-industrial complex is very complex and multidimensional and consists of public and private legal relations. The question of what is actually meant by the category of "financing" (Andreeva & Radko, 2016: 148) becomes relevant.

State funding can be provided not only through budget financing, but there are also funds, "*managed and used by public authorities and intended for financing prioritized state orientations*" (Sattarova, 2008: 8). Sovereign financial institutions are created by many states (Kudryashov, 2015: 26), although a single definition of a sovereign wealth fund has yet to be determined (Kurochkin, 2017: 54). Sovereign wealth funds can be set up in different organizational and legal forms, usually on the basis of public funding, but a mixed type of financing (public and private funding) is possible as well. The fund has no direct obligations to the source of financing, but the purpose of the fund is to meet certain public obligations.

Since June 2016 we can talk about another sovereign wealth fund of the country, which emerged as a result of separation from a state corporation called "Bank for Development and Foreign Economic Affairs"

(Vnesheconombank). It is Russian Direct Investment Fund, "*but unlike the aforementioned, this fund does not belong to the state budget category due to the specifics of its functioning*" (Shevchenko, 2017: 43). An example of this fund's projects is its investment in PhosAgro that produces apatite concentrate and is the most efficient company in the world in terms of production costs and which, consequently, potentially has the cheapest cost of fertilizers.

However, after Russia's accession to the World Trade Organization, not all forms of support are acceptable. "*Membership in the WTO imposes restrictions on the financing of programs to support agriculture*" (Zhavoronkova & Shpakovsky, 2017: 128).

At the same time, it is necessary to remember that agriculture needs additional financing because of its characteristics noted above. "*On the other hand, sanctions from some countries force the state to strengthen assistance to Russian agriculture, aiming at import substitution*" (Pryntsev, 2015: 37).

Another classification of funding according to the funding mechanism (method) has become very popular recently. This way, financing can be divided into financing of projects and financing of processes. Federal Project Office has been established in Russia to ensure the construction and management of the portfolio of priority projects (programs). According to some scientists, "*in the Russian agro-industrial complex, project financing has not yet received proper development*" (Shatokhin, Sirotkina, & Fomicheva, 2014: 20), but the topic is of interest to many economists.

Nevertheless, in the State Program for Development of Agriculture and Regulation of Agricultural Commodities Markets, financing has already been divided into project and process parts. Financing of accelerated import substitution of main agricultural products, raw materials and food, stimulation of investment activities in the agro-industrial complex, including the priority territories, is carried out according to the project method. The process method administers financing of agricultural land reclamation and sustainable development of rural areas.

However, there is no explanation of what is meant by the project method in the said document; in fact, it does not correspond to the concept

of project financing as it is conventionally defined (Kuznetsov, 2016: 26), namely the financing of a specific investment project.

First of all, the concepts of project and process financing should be clarified and used by legislative and policy documents in the same sense that economists put in them. Project financing should be used with greater breadth and precision, not only at the federal level but also at the regional and municipal levels. Prospective development trends in specific rural areas should be envisaged with the help of economists, and detailed investment projects should be developed for these projects.

Project financing is considered by specialists as a "*multi-tool form of financing*" *requiring* "*development of the methodology of project analysis, assessment of project risks, including their cost evaluation, monitoring and management*" (Nikonova, 2014: 98), as well as the development of public legal agreements and overall legal and institutional support. In some cases, the creation of a special project company (Belitskaya, 2015: 32) is also needed.

In case the state participates in the implementation of project financing of agriculture, it is possible to speak not about state support, but about the realization of another function of the state – innovative (Stepanenko, 2018: 2). Existing documents on agricultural support and investment project organization are have not yet been harmonized.

In our opinion, investment projects in the agro-industrial complex can take the following form: measures for the development of organic production in ecologically clean regions (Anisimov & Popova, 2017: 146), support of regional or local agricultural brands (Gorlenko, 2010: 3), development of clusters involving agricultural enterprises, for example, in conjunction with the production of biogas (Papenov & Kazantseva, 2016: 46), development of agricultural crowdfunding system using available facilities of the Internet (Klinov, 2018: 91; Kotenko, 2014: 140) and some other one-time projects related to sustainable development of rural areas and creation of an infrastructure to ensure a decent life for the rural population that contribute to preservation of their multi-layered economy and culture.

5 Conclusion

Over the past two decades, Russia has seen radical reforms in its economy in general and in financing of the agro-industrial complex in particular. Both budgetary and extra-budgetary funds are currently being used. Budget financing is realized in the form of state support in priority directions. Various types of subsidies granted to agricultural producers and other organizations that provide the agricultural sector with agricultural vehicles, transport, and credit funds, have been analyzed. Centralized state planning has been replaced by strategic, which is based on entirely different principles, such as the focus on future results with different scenarios of further development.

State support is being significantly reduced, although the State Program for Development of Agriculture and Regulation of Agricultural Commodities Markets provides for special sub-programs related to the need for import substitution of agricultural products in light of the sanctions imposed on Russia by certain countries.

As for the principles of financing, it is possible to highlight the obligatory co-financing both at the level of granting subsidies from the federal center to the regions and of providing funding to economic entities. One of such manifestations of co-financing is the development of public-private partnership.

Lending is considered to be the main form of financing of the Russian agro-industrial complex, although lending to agricultural producers has special features, and subsidies are supposed to be provided to authorized banks that grant preferential loans to agricultural producers.

The concept of financing has been analyzed, and grounds for classification of types of financing are identified. The underestimated potential of financing of the agro-industrial complex from sovereign funds has been revealed.

Various opportunities for applying project financing in agriculture have been investigated. Unlike process financing, in which funding is aimed at supporting processes and activities, project financing is understood by economists as the operational management of a particular project. The State Program for Development of Agriculture and Regulation of Agricultural

Commodities Markets identifies both types of financing. However, the characterization of these types in the document does not fully correspond to the generally accepted definition, which calls for clarification of the terms according to the meaning intended by the program's drafters. On the other hand, project financing in the conventional sense could be an excellent complement to process financing in the realization of investment projects in the agro-industrial complex, but implementation of this type of financing requires the development of a common conceptual framework and principles, as well as institutional and contractual modalities.

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PART 4:
FINANCIAL LAW
OF THE EUROPEAN UNION

Cohesion Policy in the Light of Public Finance

Romana Buzková[1]

Abstract

This contribution deals with the European Union's cohesion policy. The aim of this paper is to confirm the hypothesis that this policy serves as an important investment tool of EU public finance. The methods of description, analysis, comparison and synthesis are used for achieving this aim. By using statistical data regarding GDP, the paper focuses on regional disparities in the EU and the Czech Republic.

Keywords: Cohesion Policy; European Union; Funds; Public Finance.

JEL Classification: O1; R1.

1 Introduction

Cohesion policy is one of the most visible policies of the European Union due to its results that are delivered close to the citizens, especially in countries like the Czech Republic which are net beneficiaries of EU funding. Therefore, I present some of the achievements in this paper as well. The main aim of this contribution is to define the role of cohesion policy in the context of public finance while paying special attention to regional aspects of this policy. The aim is to confirm or disprove a hypothesis that the policy serves as an important tool of EU public finance. The scientific methods of description, analysis, comparison and synthesis have been used for writing this research paper.

The next chapters deal with the concept of public finance, theoretical and practical background of the European Union's cohesion policy, its impact and results, and future challenges followed by conclusions.

This paper has been prepared as an outcome of the research project MUNI/A/1456/2018 which deals with the evolution of public finance in selected countries and its legal context.

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2 Public finance

A single definition of public finance does not exist. The term "finance" can be defined as social relationships of its kind whose object are funds in various forms. These relationships are associated in particular with the implementation and use of money funds. Finance can be divided into public and private. Public finance involves a wide range of state and other public corporation activities, their bodies and other subjects, inexhaustible number of links and relations between them but also towards private individuals. Such activities and links are related to the creation, distribution and redistribution of public funds. It is also interesting to assess finance from their object point of view; if the object is public money, we can talk about financial relationships as part of public finance (Mrkývka et al., 2014: 10–15).

Nowadays, public finance goes beyond national borders and reaches a supranational level. Public finance in the international context includes monetary relations arising from the collection, distribution, redistribution and use of money. International public finance includes transfer payments and is based on the same principles as national public finance; the most frequently mentioned example of a transnational budget is the budget of the European Union (which manages its own resources and creates several other funds where the principle of co-financing is applied). This budget is derived from national public finance but at the same time possesses autonomy. The fiscal allocation thus takes place both at national and transnational level (Tomášková, Pařízková, 2015: 24–25).

2.1 Legal background

Article 174 of the Treaty on the Functioning of the EU states that "*in order to promote its overall harmonious development, the Union shall develop and pursue its actions leading to the strengthening of its economic, social and territorial cohesion. In particular, the Union shall aim at reducing disparities between the levels of development of the various regions and the backwardness of the least favoured regions*".

Cohesion policy is currently delivered through three main funds; the European Fund for Regional Development (EFRD), the European Social Fund (ESF) and the Cohesion Fund (CF). Together with the European

Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF) they form the European Structural and Investment Funds (ESI Funds) in the programming period 2014–2020. The rules for the functioning of ESI Funds are currently governed by the Regulation (EU) No 1303/2013 (common provisions regulation). In addition, each fund is a subject to its specific regulation which further determines the scope of the fund.

3 Classification of regions

Characterising European regions is an extremely difficult task resulting from significant differences in their legal status, organisation, administration, competencies and so on. Something that is understood as a region in one country is called a district or a county in another; or some concepts of the same name have different functions in various countries or serve only as artificial administrative creation for the purposes of NUTS (Sowiński, 2018: 616).

The NUTS (Nomenclature of Territorial Units for Statistics) system has been developed by the European Union mainly for the assessment of eligibility for EU funding. The three-level regional hierarchy is based on minimum and maximum population thresholds (see table 1).

Table 1: NUTS classification – general overview

Level	Description	Minimum population	Maximum population	Number of regions
NUTS 1	Major socio-economic regions	3 million	7 million	104
NUTS 2	Basic regions for the application of regional policies	800 000	3 million	281
NUTS 3	Small regions for specific diagnoses	150 000	800 000	1348

Source: author (based on Eurostat data)

Regions eligible for support under cohesion policy have been defined at NUTS 2 level. There are three categories of regions: less developed

regions, transition regions and more developed regions. The main criterion for such division is regional GDP per capita (see table 2). Although all regions can benefit from EU funding, the biggest share of financial support is set aside for less developed regions.[2]

Table 2: Division of NUTS 2 regions

Category	GDP per inhabitant
Less developed regions	< 75 % of the EU average
Transition regions	75–90 % of the EU average
More developed regions	> 90 % of the EU average

Source: author (based on Eurostat data)

In the Czech Republic, there is one NUTS 1 region, eight NUTS 2 regions and fourteen NUTS 3 regions (see table 3).

Table 3: NUTS classification – Czech Republic

NUTS 1	NUTS 2	NUTS 3
Česká republika (Czech Republic)	Praha (Prague)	Hlavní město Praha (Prague capital city)
	Střední Čechy (Central Bohemia)	Středočeský kraj (Central Bohemian Region)
	Jihozápad (Southwest)	Jihočeský kraj (South Bohemian Region)
		Plzeňský kraj (Plzeň Region)
	Severozápad (Northwest)	Karlovarský kraj (Karlovy Vary Region)
		Ústecký kraj (Ústí and Labem Region)
	Severovýchod (Northeast)	Liberecký kraj (Liberec Region)
		Královéhradecký kraj (Hradec Králové Region)
		Pardubický kraj (Pardubice Region)
	Jihovýchod (Southeast)	Kraj Vysočina (Vysočina Region)
		Jihomoravský kraj (South Moravian Region)
	Střední Morava (Central Moravia)	Olomoucký kraj (Olomouc Region)
		Zlínský kraj (Zlín Region)
	Moravskoslezsko (Moravian-Silesian)	Moravskoslezský kraj (Moravian-Silesian Region)

Source: author (based on Annex 1 to Regulation (EC) No 1059/2003)

2 Exception: eligibility for the Cohesion Fund is based on a country's GNI, not regional GDP. Member States with a GNI per capita below 90 % of the EU average are eligible for funding.

4 Distribution of funds

The total amount dedicated to cohesion policy in the 2014–2020 programming period is 351,8 billion EUR (the total EU budget is 1082 billion EUR). When it comes to the management of funds, the European Commission shares competence with the Member States. In a nutshell, each Member State has to draw up a Partnership Agreement which includes details regarding operational programmes, investment priorities and development needs. The Commission approves all agreements while playing a supervisory role. Operational programmes are managed (and individual projects selected) directly by managing authorities in the Member States. Potential beneficiaries include public bodies, enterprises (especially SMEs), universities, NGOs etc. Depending on the division of regions (see chapter 3.2), funds can provide up to 85 % of the project costs. The remaining financing comes from public or private sources (European Commission, 2014).

5 Impact and results of the policy

The overall financial impact of cohesion policy in the 2014–2020 programming period is expected to be around 450 billion EUR, taking into account national contributions and other private investments. (European Commission, 2014).

Every three years, the European Commission shall submit a report (so-called Cohesion report) which monitors the progress towards achieving economic, social and territorial cohesion. The report shall be accompanied by appropriate proposals if necessary. It is submitted to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions (Article 175 TFEU).

Seven Cohesion reports have been published so far. They asses the socio-economic situation in EU regions, analyse the impact of policies and taken measures, provide detailed statistical data regarding e.g. GDP, public investment, employment etc.

The latest Seventh report on economic, social and territorial cohesion, which was published in October 2017, fulfils two requirements; it presents

its findings on how the EU regions evolved (based on the assessment of national policies, cohesion policy and other EU policies) and reviews the measures that link the effectiveness of ESI Funds to sound economic governance.[3] This review was required by Article 23 of Regulation (EU) No 1303/2013: *In 2017, the Commission shall carry out a review of the application of this Article. To this end, the Commission shall prepare a report which it shall transmit to the European Parliament and the Council, accompanied where necessary by a legislative proposal.* Such legislative proposal was not deemed necessary by the Commission.

According to this report, cohesion policy provides funding equivalent to 8,5 % of government capital investment in the EU. This number rises to 41 % for the Member States which joined in 2004 and 2007 (and to over 50 % for a number of countries, for example Portugal, Croatia or Lithuania). The impact of cohesion policy on EU economies is very important and the effects of investments build up over the long term. For countries that have joined the EU since 2004, it is estimated that investments for the 2007–2013 period increased their GDP by 3 % in 2015, and by a similar amount for the 2014–2020 period in 2023.[4] This has contributed to a significant convergence of GDP per capita in these countries which increased from 54 % of the EU average in 2006 to 67 % in 2015.

6 Regional disparities and (un)employment

The economic crisis in 2008 and 2011 seriously affected almost all Member States which stopped the long-term reduction of regional disparities in GDP per capita (and in some cases the disparities even widened). In 2014, disparities in employment started to narrow, followed by disparities in GDP in 2015. However, many regions still had these rates below pre-crisis levels. More developed regions (above the EU average) have grown faster than less developed regions.

3 These measures provide the Commission with the power to request changes in programmes to address economic policy priorities recommended by the Council and the obligation to suspend the funds in cases of non-effective action by the Member State to address an excessive government deficit or excessive macroeconomic imbalance.

4 Including Croatia which joined in 2013.

In 2016, with 71 % the employment rate exceeded the pre-crisis level for the first time. The unemployment rate has fallen from a high of 10,9 % in 2013 to 8,6 % in 2016. In January 2019, the unemployment rate of EU-28 reached a record low level with 6,5 %. However, a lot of young people under the age of 25 still face problems to find a job. In December 2018, the youth unemployment rate was 14,9 % with the lowest rate in the Czech Republic 5,8 % and the highest rate in Greece 38,5 % (Eurostat, 2019).

Some regions face rapid population growth while others depopulate. The big differences in job opportunities and income across the EU encourage people to move. In several regions, this has led to rapid changes in population, which has put pressure on public infrastructure and services. Integrated strategies can make a great impact. In cities for example, improving urban transport can reduce congestion, make companies more productive and also connect deprived neighbourhoods (European Commission, 2017).

7 Investments

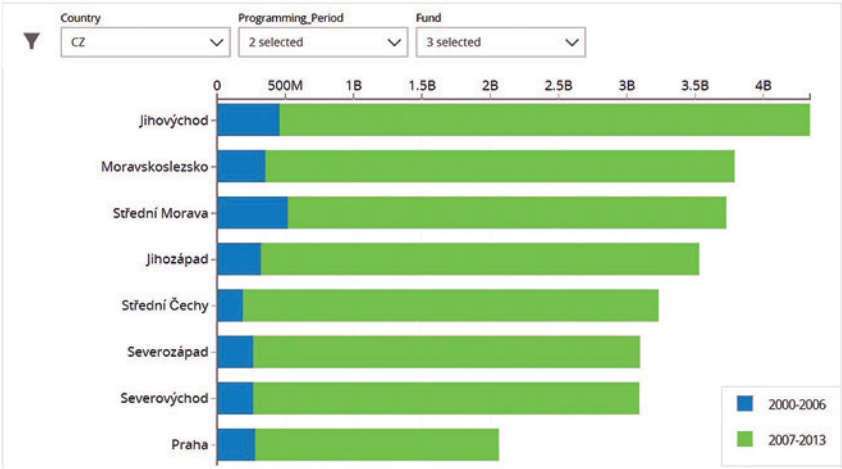
Public investment still shows major gaps between Member States. Investments in innovation remain highly concentrated in a limited number of regions (northern and western Member States) whereas the innovation performance in southern and eastern Members States is weaker. More investment will be needed to complete the TEN-T transport network. Investments in energy efficiency, renewable sources of energy and low-carbon means of transport will be also needed, although Member States either already reached or are close to reaching their 2020 targets. The programmes in the 2014–2020 period also plan to support more than 1 million SMEs, leading directly to the creation of 420 000 new jobs, further invest in digital economy, social infrastructure, territorial cooperation etc. (European Commission, 2017).

8 Czech Republic

In April 2018, the European Commission published its most comprehensive historical record of the EU budget payments from EU funds to Member States and NUTS 2 regions. Thanks to this data, it is possible to answer

a difficult question of how much regions and countries have received under cohesion policy funding. Table 4 (see below) provides an overview for the Czech Republic and includes two programming periods and three funds (ERDF, CF, ESF).

Table 4: EU payments to the Czech Republic, in EUR



Source: European Commission

In the 2014–2020 period, the Czech Republic manages eight operational programmes under cohesion policy out of ten operational programmes in total. The total sum of nearly 24 billion EUR was allocated from all five ESI Funds (including EAFRD and EMFF) with almost 22 billion EUR dedicated to cohesion (EFRD, CF, ESF). Additional resources are available in European Territorial Cooperation programmes (European Funds Portal in the Czech Republic, 2018).

For the 2014–2020 period, all regions except Prague are eligible for EU funding as less developed based on their GDP per capita. Regarding the latest GDP developments, Prague is still the only region in the Czech Republic that has GDP per capita significantly above the EU average (being the only more developed region according to NUTS 2 classification). Four regions are currently in the transition category and three regions are considered as less developed with GDP below 75 % of the EU average (see table 5).

Table 5: Regional GDP in the Czech Republic, 2017

Region	Total GDP € million	Share in national GDP %	GDP per inhabitant € / PPS	GDP per inhabitant %
European Union	15 383 066		30 000 / 30 000	100 %
Czech Republic	191 722	1,2 %	18 100 / 26 900	89 %
Praha	48 751	25,4 %	37 900 / 56 200	187 %
Střední Čechy	22 784	11,9 %	16 900 / 25 100	84 %
Jihozápad	19 090	10,0 %	15 700 / 23 300	77 %
Severozápad	14 315	7,5 %	12 800 / 19 000	63 %
Severovýchod	22 981	12,0 %	15 200 / 22 600	75 %
Jihovýchod	27 760	14,5 %	16 400 / 24 400	81 %
Střední Morava	18 024	9,4 %	14 800 / 22 000	73 %
Moravskoslezsko	18 017	9,4 %	14 900 / 22 100	74 %

Source: author (based on Eurostat data in purchasing power standards)

9 Future challenges

The European Union is currently facing a number of challenges. The most visible and heavily discussed is the United Kingdom's intention to withdraw from the EU (Brexit) which is also linked to the ongoing negotiations regarding the multiannual financial framework 2021–2027. Based on their outcome, it will become clear whether the solution prepared for the EU-27 will be adopted. The European Commission introduced its legislative proposal on future long-term EU budget in May 2018.[5] The overall budget allocation for economic, social and territorial cohesion in the 2021–2027 programming period is proposed as 330 642 million EUR.

In the 2021–2027 period, cohesion policy will keep on investing in all EU regions. The core elements of the allocation of funding remain the same (still largely based on GDP per capita), however, new criteria are added: youth unemployment, educational attainment, greenhouse gas

5 Proposal COM(2018) 322 final for a Council Regulation laying down the multiannual financial framework for the years 2021 to 2027.

emissions and migration. Regarding the three categories of regions, there are two key differences proposed. First, in the anticipation of Brexit, the EU average of 27 Member States is used for the GDP calculation (and not EU-28). Second, transition regions category has widened and should include regions with GDP between 75 and 100 % of the EU average (Bachtler et al., 2018: 30–31, 26–37).

To boost economic development and the impact of cohesion policy in EU regions, the efficiency and transparency of public institutions as well as justice systems need to be improved. Cohesion policy should also become more flexible and be able to respond to new challenges more quickly while ensuring complementarity between financial instruments (European Commission, 2017).

In order to simplify the rules for managing authorities and beneficiaries, the Commission proposed a new single set of rules for all EU shared managed funds in May 2018.[6]

10 Conclusion

The objective of the paper was to confirm or disprove the hypothesis whether cohesion policy serves as an important investment tool of EU public finance. Based on the presented research outcomes, it is possible to confirm this hypothesis. The allocation of public funds takes place both at EU level (transfers from the EU to Member States) and national level (transfers to end recipients – beneficiaries). Cohesion policy functions as a catalyst for further public and private investments due to its national co-financing obligation. The main results regarding GDP per capita show that a significant improvement has been achieved in countries that joined the EU in 2004 and later. However, regional disparities still remain, e.g. in the area of youth employment.

6 Proposal COM(2018) 375 final for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument.

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Proposal COM(2018) 375 final for a Regulation of the European Parliament and of the Council laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, and the European Maritime and Fisheries Fund and financial rules for those and for the Asylum and Migration Fund, the Internal Security Fund and the Border Management and Visa Instrument.

Regulation (EC) No 1059/2003 on the establishment of a common classification of territorial units for statistics (NUTS), as amended.

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The Role of European Commission Decisions for Implementation of State Aid Rules in Taxes

Anna Dobaczewska[1]

Abstract

In this paper I will try to answer the question whether numerous EC decisions adopted or being (currently) under ECJ appeal procedure will change considerably the way the notion and range of state aid is understood, especially in taxation. The main aim of this paper is to confirm that it were the EC decisions that contributed the most to the current definition of state aid, not the EU legislation. I will focus on the element of selectivity and distortion of trade between Member States. It seems that although the latest EC decisions regarding tax regulations have been broadly discussed; and considered by many as controversial, they will not notably change the attitude of the EU court presented so far, but have and will influence the national legislation. This has been evaluated mainly on the analysis of jurisprudence and analysis of soft law acts. It is to be expected, that (following the notice of state aid as of 2016) the ECJ will confirm the broad perception of state aid definition, provided by the Commission, especially with regard to the feature of selectivity.

Keywords: Tax; Law; State Aid.

JEL Classification: H25.

1 Introduction

Though the tax policy and legal solutions of direct taxes are subject to independent national legislation, they are significantly influenced by competition

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regulation of the EU. The aim of this article is to show and analyse how the EC decisions based on the regulation of (currently) art. 107 and art. 108 TFEU have stamped its mark on the taxation policy and legislation of the Member States, especially during the last few years. The Member States needed to reconsider and change (not always voluntary) some of their tax solutions in order to comply with the EU competition rules. The definition of state aid refers to several conditions, which (if met) constitute a state aid instrument. These being: (i)state resources, used in order to grant a (ii) selective (iii) advantage, favouring certain entrepreneurs or production of goods, which (iv) distort the competition and affects the trade between member states (Lyal: 1028).

2 The role of taxation in competition

EU Member States, as many others countries, compete with each other for foreign direct investments. One of the methods is lowering their tax rates for foreign investors and provide them with some tax deductions. The taxation policy and legislation is at least as valuable instrument of competition as low wages, good transport infrastructure or a significant demand on the market in question. Therefore it may be considered as justified that several EU members states include in their tax systems provisions that attract (especially foreign) investors, by lowering tax rates or allowing for taxable profit shifts in case of holding groups. The primary goal of those rulings lays indeed in the desire to promote and attract foreign direct investments, and not to disrespect competition rules. However, according to an opinion of the EC authorities those (and other) taxation instruments may also contribute to an anticompetitive practice among the Member State and influence the internal market in a negative way; which on the other side constitutes illegal state aid according to art. 107 TFEU.

On the other side the Member States have been equipped in power to establish a sole and independent tax policy in direct taxes. The main question today is therefore whether the ECJ will decide that it is still the Member States' autonomous power in taxation policy that prevails, or that the competition rules must be obeyed first, when constructing tax solutions constituting an incentive for international direct investments.

While the original purpose of state aid legislation was to prevent Member States from subsidising their own "national champions" and limiting competition from companies located in other Member States, the concept has evolved to include a longer list of numerous state incentives attracting companies from third parties. The many considerations entrepreneurs need to make, before choosing the country of residence, include the legal form of activity, the choice between operating as a subsidiary or as a branch. Their answer lays very often in the taxation level and in the possibility for the taxpayer to receive upfront some reassurance that its' planned international model of economic activity (which provides for a decrease of tax obligations) will be accepted by the tax authorities. Some countries allow tax payers to gain more certainty about their future taxation by issuing some binding and/or non-binding interpretations, rulings or even individual agreements giving the investors comfort on their taxes. It refers mainly to international and in intergroup relations of capital holdings (within and outside the borders of the UE) who may obtain tax rulings or transfer pricing arrangements from national tax authorities. In such a case it definitely has influence on the internal market and trade between Member States. This is the reasoning behind the cases brought before the European Commission in the last few years. Once the tax incentives would be terminated as form of state aid, and not considered as an instrument of direct taxation policy, the foreign investors may retreat from the investment. In countries highly relying on foreign capital (like Luxembourg or the Netherlands) a dramatic change of tax policy may destabilise their economies as a whole.

The final statement is not only important for the investment from the perspective of the country in question. Also the European Union as a whole is keen to promote inbound foreign investments. This is a necessity, in the light of the fact that the EU internal market has been confronted with strong competition for instance from the US or the BRIC countries. This has led to numerous EC decisions striving to obtain harmonised rules on taxation as a competition tool and considering the internal market as one, homogeneous, relevant market, where national tax incentives should be considered as anticompetitive, illegal state aid. The European Commission exercised quite a number of controls over the taxing power of Member

States. Following to that the EC imposed restrictions on national direct taxes in several cases. It's done not by way of regulating the taxes, but by the application of the competition rules.

3 The role of the European Commission decisions in creating national taxation systems

Since the introduction of the EU internal market, the activity of the European Commission referring to state aid has mainly focused on the elements of state aid definition (as included in art. 107 TFEU); like selectivity and preferential treatment, the influence of fiscal solutions on trade between the Member States. The dilemmas have been solved step-by-step in EC decisions and by preparing soft law acts, like notices explaining the EC point of view on the scope of state aid. The fact that tax preferences may constitute some kind of state aid, as indirect engagement of public means has been clear at least since the notice on the notion of state aid from 1998.

Since the 1990ies the EC regularly checks on the practises of the Member States in respect of state aid forms and conducts regular surveys on the topic (like the 6th Survey on State Aid in 1998). Those surveys show i. a. the budgetary expenditures and amounts distributed as tax allowances in particular countries and in the whole EC. In 1998 the Commission issued its first "Notice on the state aid definition" and established a systematic approach allowing the EU to create their policy towards i.a. taxation preferences in compliance with the Treaty provisions. This notice provided for a rather broad definition of illegal state aid and gave small limits for implementation of tax solutions as an investment incentive. First of all, the above mentioned notice clearly confirmed that resignation of tax revenues is equivalent to consumption of State resources, and for that reason possibly a form of state aid. It also confirmed that the EU has the power to eliminate any provisions that harm the internal market, by issuing decisions on unlawful selective advantages, also as regards direct taxation. The selectivity may be easily noticed, but also hidden.

Through the years the European Commission kept searching for instruments that constitute illegal state aid in tax regulations. Sometime later, enriched

by quiet a number of ECJ judgement and own decisions (to be presented in detail beneath) the Commission published in 2016 another notice referring to the definition of state aid; presenting the Member States an updated EC position in this respect. It encompassed also tax rulings, transfer pricing agreements and other individual preferences. The notice refers to individual tax preferences and giving the international investors incentives. The European Commission made clear that both general and individual taxation solutions may be considered as anticompetitive. Any, sometimes highly sophisticated, forms of relief, giving the investors comfort that their profits will be taxed with lower tax rates as in another country will be considered as state aid. This applies not only to individually defined companies and/or holdings, but also to some narrow group of enterprises.

As indivual state aid has become a very popular economic instrument, eagerly used by Member States in hidden forms, the Commission decided to present all MS a questionnaire about national tax law and tax rulings. It has initiated (in June 2013) an investigation on whether and what kind of legal solutions in each Member State exist, regarding forms of tax privileges, gaining any kind of tax certainty, issuing tax rulings and/or the possibility to execute advance pricing agreements, which give preferential treatment only to certain companies. The survey looked for binding and non-binding instruments, notwithstanding whether those have a formal character (like an administrative decision) or are rather closer to a gentlemen's agreement[2]. Notwithstanding its formal character each such ruling causes comfort for the entrepreneurs receiving it, that their taxes will not be questioned by national authorities. Depending on the country in question, such rulings are available to all tax payers or to a selected group of them (mainly large companies planning investments). None the less it will have selective character as soon as an individual submits an application.

2 Simultaneously to the EU, the OECD also works on documents aimed at gaining transparency in taxing of international business and seeks for recipes on tax avoidance (on BEPS – base erosion and profit shifting). The OECD documents, such as the consensus from 2015 reached at the G20 meeting have already been an inspiration for the EU authorities.

Having gathered much more experience, and as a result of a modernisation process[3] of state aid, commenced parallel to the enquiry in 2012, the EC concluded that to some extend also individual tax rulings and tax agreements between tax payers and tax authorities indeed constitute state aid. However each case should be examined individually. In any event the indirect selective advantage should be proofed to exist, unless it is selective *prima facie*.

4 The main EC decisions and ECJ judgements on taxation regulation constituting state aid

During the last decades the European Commission has issued many notices, documents and decisions, (some of which have been appealed to the European Court of Justice) which built a consistent and consequent picture of what is, and what is not considered as compatible with the internal market, regarding tax solutions. Those decisions created a playing field on which the Member State may try to establish national tax regulations without the accusation of imposing selective advantages for a group or even for individually defined entrepreneurs.

Many of the EC decisions dealt particularly with the topic of selectivity of taxation regulation. From the Court's case-law it clearly derives that it confirms the EC point of view on the feature of selective support, granted by public means together with the delimitation of a category of undertakings which receive a tax advantage. One of the examples will be the *Adria Wien Pipeline* case (case C-143/99, EU:C:2001:598)[4] The ECJ shared the EC opinion, and raised no doubt that the selectivity is present, as soon as the tax refunds are available only to those entrepreneurs who submit an application; even if the possibility to submit such an application is open to every entrepreneur meeting legal conditions. Granting some tax rebates wouldn't constitute a selective means, only if the rebates were made available to all companies active on the territory without any distinction, including the scope of business.

3 Communication on State Aid Modernisation (SAM), Brussels 8. 5. 2012, COM (2012)209final, which launched a major state aid reform, by making incentives focused on main EU strategical topics, becoming more efficient and timely enforced.

4 W. Nykiel, A. Zalasinski, Orzecznictwo Trybunału Sprawiedliwości UE w sprawach podatkowych.Komentarz, Warszawa 2014, p. 838.

In another judgement, as of 15 November 2011, (*Commission and Spain v. Government of Gibraltar and United Kingdom* C106/09 P and C107/09 P, EU:C:2011:732)[5], the ECJ confirmed that the selectivity of a tax measure can be established even when that measure does not constitute a derogation from an ordinary tax system, but is an integral part of that system, differentiating the taxation of certain groups of tax payers. Such a conclusion is important for the Member States willing to proof that, when a measure establishes a derogation from the ordinary tax system, it is not selective. In the abovementioned case the ECJ judged that when the benefits of a taxation derogation aim only at certain operators and not others, although all those operators are in an objectively comparable situation in the light of the objective pursued by the ordinary tax system, the derogation is selective.

In many similar cases, ECJ has decided that the advantage concerned also is selective, if it is for the benefit of: undertakings belonging to a single economic sector and carrying out particular transactions (like in judgment of 15 December 2005, *Unicredito Italiano*, C148/04, EU:C:2005:774); undertakings resident for tax purposes outside the territory of a region (judgment of 17 November 2009 *Presidente del Consiglio dei Ministri*, C169/08, EU:C:2009:709); or even undertakings that have a particular legal form (judgment of 10 January 2006, *Cassa di Risparmio di Firenze and Others*, C222/04, EU:C:2006:8). Finally also in the case when the selective only undertakings of a certain size (judgment of 13 February 2003, *Spain* v *Commission*, C409/00, EU:C:2003:92).

One of the latest ECJ judgements (as of 21 December 2016, joint cases C-20/15 P Commission v. World Duty Free Group SA, and C-21/15 P *Commission v Banco Santander and Santusa*; EU:C:2016:981) should have been taken under consideration by the Polish legislator when it was proceeding on the Act on taxation of retail sales.

The initial EC procedure on state aid, was actually commenced in 2009. Since the case C-20/15 referred to an earlier judgement in case known as *Autogrill España SA* (T219/10, EU:T:2014:939), in which the Commission also contested the right for tax amortisation of financial goodwill. Such

5 W. Nykiel, A. Zalasinski, Orzecznictwo Trybunału Sprawiedliwości UE w sprawach podatkowych. Komentarz., Warszawa 2014, p. 852.

a right was established by Spain only for foreign shareholding acquisitions. One of the provisions questioned by the Commission in all three above mentioned cases was the selective nature of the taxation provisions, constituting an abberation of the "normal" tax system. The EU law puts an obligation on the Commission to identify the ordinary or 'normal' tax system applicable in the Member State concerned, and afterwards to give evidence that the tax measure at issue is a derogation from such an ordinary system. Tax payers who, in the light of the objective pursued by that ordinary tax system, are in a comparable factual and legal situation must be treated equally by law. The Commission knowing that the tax deduction was applicable only to residents who acquired at least 5 % shareholdings in foreign companies, found that the the consequence of that measure was that resident undertakings were not treated equally. The measure at issue stated that, to be classified as a 'foreign company', a company must be liable to pay a tax that is identical to the tax applicable in Spain and its income must derive mainly from business activities carried out abroad. The EC decided, that the fact that the number of undertakings able to claim entitlement under a national measure is very large, or that those undertakings belong to various economic sectors, is not sufficient to disclaim selectivity.

Some of the mentioned circumstances creating selectivity is correntlly subject to ECJ considerations regarding the Polish Act of 6 July 2016 on taxation of retail sales. Soon after the legal act was issued by the Polish Parliament, the Commission (case SA.44351, decision of 30. 6. 2017, EU:L:2018:29) questioned the progressive tax rates relating to the turnover of taxpayers. The progressive rate structure includes three different brackets and rates depending on the value of turnover[6], and in practise the size of the entrepreneurs determines the amount of levy due. Poland could not present any convincing arguments to the EC, why larger and smaller retail operators are

6 The Act included three different monthly turnover brackets subject to three different tax rates: a tax rate of 0 % on the amount of monthly turnover from retail sales not exceeding PLN 17 million; a tax rate of 0,8 % on the amount of monthly turnover over PLN 17 million but not exceeding PLN 170 million; and a tax rate of 1,4 % on the amount of monthly turnover from retail sales above PLN 170 million. This would lead to significant differences of effective tax rate for smaller and/or foreign entrepreneurs, and therefore be selective (EC decision (EU) 2018/160 of 30 June 2017 on the State aid SA.44351 (2016/C) (ex 2016/NN) point (16).

in a different factual and legal situation as comes to the tax amount due. So a justified exemption from the reference tax system was not successfully prooved.

After an in-depth investigation the Commission confirmed that the progressive tax rates granted are a *prima facie* selective advantage to companies with low turnover over their competitors, and therefore the proposed legal structure constitutes an illegal form of state aid (especially for small and medium enterprises). The Polish representatives could not proof that the bracketed progressivity would not emcompass any selective advantage, only because the same rate schedule applies to all retail undertakings reaching the same level of turnover and all entrepreneurs, no matter the size of it. In the opinion of the Polish party all entrepreneurs active on the polish territory are in the group of potential beneficiaries to be compared with one another. The EC contested however the Polish point of view, and considered that the reference system within which tax rates should be compared is not only the group of entrepreneurs having revenues higher than 17 mil. PLN, but all enterpreneurs, regardless their total revenues. The progressive tax rate structure introduced by the Act should be regarded, in the EC opinion, to be specifically designed to favour smaller retailers over larger ones by applying different tax rates for both groups. The EC has even presented a simulation of revenues and tax rates, clearly showing that the effective tax rate is discriminatory to the bigger enterprises (holdings).

In fact, the vast majority of undertakings operating on the retail sector in Poland fall below the threshold and will be exempted. The obligation to pay the retail tax would be put only on several, mainly foreign-owned, sale companies. In the opinion of the Commission the fact that a vast majority of entrepreneur will be exempted does not abolish the selective nature of the provisions. The EC also noted that the selectivity can harm retailers operating as part of a holding structure, opposite to those operating as franchisees. The advantage to individual retailers operating as franchisees is granted, since their tax burden is determined on the basis of their individual stores' monthly turnover from retail sales, rather than on the basis of the entire chain's monthly turnover from retail sales, as it is the case for retail chains operating under a holding company model. Poland didn't succeed to demonstrate

that the tax measures were justified by the nature or general scheme of the tax system, either. In the light of arguments brought by the EC in the above-mentioned Gibraltar-case, it is also highly unlikely, that the regulation will be considered as justifiable by the ECJ. The Polish party did not present in the appeal any arguments, which weren't known from previous ECJ cases. Therefore it is to be expected that the ECJ judgement (yet to come), will consider the Polish tax regulation on retail sales as illegal state aid.

It is worth mentioning that because of the EC decision, and ECJ procedure pending the enforcement of the Act was postponed by the Polish government twice: first until 1 January 2019 and is now planned to come into force at 1 January 2020. However, keeping in mind other previous cases, one can expect that the Polish parliament will be forced to repeal the Act completely, once the ECJ judgement is issued.

The EC has lately dealt with other cases in which the tax rates were differentiated in order to protect or even to favour domestic entrepreneurs (especially those micro, small and medium sized). This was the case with the Hungarian food chain inspection fee and tax on tobacco sales. On 4 July 2016, the Commission found those levys as incompatible with EU state aid rules (SA.40018, SA.41187)[7]. The Commission considered that the progressive rate structure provides a selective advantage to companies subject to the lower rates (those with lower turnover), and discriminated the bigger market-players. Following that, the Hungarian Parliament abolished the progressive rates structure and re-introduced the flat rate for all food chain operators.

The structure of the fee obligation was quite similar to what the Polish retail tax is composed of. Therefore it should have been an indication for the Polish government to refrain from issuing a tax, based on a progressive tax rate, and distinguishing the tax payers additionally by the volume of their turnover. The Polish government, who prepared a draft of the law in February 2016, should have been aware not only of the well settled case law, but also of the EC latest decisions. The Polish authorities should have abstained from issueing the Act on retail sale taxation as a whole.

7 On 4 November 2016 the European Commission stated also that the progressive rates of the Hungarian advertisement tax (SA.39235) were distorting the competition rules and demanded its repeal and recovery.

5 Tax ruling as state aid instruments

The competences of the European Commission in respect to direct taxation in the Member States are rather scarce. It has been frequently reminded that the Member States are authonomous in the sphere of direct taxation, and they often do use the taxation as an incentive to promote investments on the national market. However, when a Member State grants individual (and therefore selective *per se*) favourable treatment to companies, by approving e.g. income transfers or giving advance certainty within a group of connected companies, it may lead to distortions of competition between the Member States (see Notice on state aid notion 1998).

Therefore it is the DG Competition who took upon the duty to protect the internal market and it searches for state aid elements in tax rulings in all Member States. The first attempts to eliminate state aid from direct taxation took place in 2001–2003. As an example: the EC examined tax ruling and transfer pricing agreements in the Belgian tax ruling scheme for foreign subsidiaries (Commission Decision 2004/77/EC, EC:L:2004:23). The Belgian tax authorities allowed for a method of determining the taxable profit of foreign (US-based) taxable entities. This aberration led to a significant decrease of tax duties of Belgian subsidiaries of US investors, whereas other foreign entities had to pay a higher tax rate. Hence, the transfer pricing agreement was selective and negatively influenced the trade between the Member States (Lyal: 1019). It forced Belgium to change their tax law and to comply additionally with the OECD guidelines on transfer pricing[8].

The EC emphasises in its decisions also the necessity of applying the arm's length principle between the companies constituting a holding group. As a result of an EC investigation in 2013 it turned out that the Member States reported all kinds of tax rulings, provided for according their national law, and being alleged state aid forms. As a result the EC has raised doubts in quite a number of them and opened in-depth investigations, mainly regarding transfer pricing agreements. Among the most publicly known are the cases of *Apple* (ECJ case in progress T-892/16), *Amazon*

8 In case of transfer pricing agreements, the EC refers to the provisions of OECD Transfer Pricing Guidelines, providing for five different method allowing to determine the equivalent arm's-length prices, with which the transfer prices may be compared with.

(ECJ case in progress T-318/18), and *Starbucks* (ECJ case in progress T-636/16).

The dispute is based i.a. on two elements. First, the burden of proof that the arms' length principle has been violated, whereas the Commission seems to impose its own interpretation of the arm's length principle on Member States, while the OECD guidelines are available. It should not be forgotten that in previous cases on alleged state aid in transfer pricing the EC based its decisions on OECD guidelines in this respect, and there is no reason why it would refrain from them in the present cases. Second, that the EC should safeguard the legitimate expectation of the tax payer, that the agreements on tax ruling are respected. As a matter of fact this has been rather rarely the case (Giraud, 2008: 1399); as the EC ordered in all finished cases full recovery of the advantages received through the years. (the EC also estimated the amounts to be recovered).

The EC approach towards the calculation of income and costs based on the arm's lenght principle has been confirmed in the Notice of the Commission on the notion of state aid in 2016. It refers to the OECD guidelines itself and to the assessment methodology, considered as a guarantee for an outcome in line with market conditions. In the Amazon case the EC imputed that none of the methods were used while agreeing on a tax ruling. The EC also put forward that no test on comparability of the rulings' tax rate with any reference system took place. Indeed, Luxembourg allowed two Amazon holding companies to shift their profits to a US-based company, and where those companies defer to pay any taxes, notwithstanding the fact that this US company has not been involved in real business. So additionally such an arrangement on transfer pricing led to illegal tax avoidance. This is why the tax payers may not have any legitimate expectations that the ruling stays in force.

The same avoidance effect can be noted in the Irish *Apple* case. The EC displayed that the effective tax rate, because of profit shifting, was practically eliminated, as it decreased from 1 % to 0,005 %. In this case however, the Commission raised doubts not about the calculation method, but the period (lasting since 1991) for which the ruling was granted.

Following to the EC procedures (in progress are *Fiat, Engie, McDonald)*, and not awaiting the effects of appeal to ECJ, Luxembourg has implemented a new law on transfer pricing. It formalizes the arms' length principle for the first time directly in Luxembourg national law and elaborates on the calculation methods (Hoor, O. R. 131–132). Even if the ECJ judgement would be positive for Luxembourg, it will be pointless for the future. The pressure of the Commission proved sufficient for at least one Member State to comply with the competition regulations in taxation.

The EC investigation on tax rulings contributed additionally to more transparency in taxes. As one of the consequences the EU adopted in 2016 the Anti-Tax Avoidance Directive, which ensures that binding anti-abuse measures are applied in the Member States.

As mentioned earlier of a legal solutions seems to be selective prima facie, the EC still needs to proof that it is an aberration from a reference system. In each of the latest cases under discussion the selective nature is not under question, as the rulings have been issued in favour of an individual enterprise and its subsidiaries or holding companies. The question to be answered is what (or who) is the reference system and whether the exemption can be justified. The EC could qualify any ruling as illegal state aid by manipulating with the scope of the reference system.

6 Conclusion

As presented in this article the argumentation of the European Commission regarding the selectivity of certain taxation regulations has evolved through the years, squeezing more and more the opportunities of the Member States to create their own taxation policy. The main reason for that was (and still is) to countervail distortions of competition. This refers in particular to the implementation of state aid defined i.a. as any fiscal instruments of selective nature. The competition and internal market have priority before the freedom of Member States to create their own taxation policy, as an investment incentive. Though the EC has undertaken its' survey on procedures to maintain fair competition, the outcomes also contribute to taxation policy and, especially to the elimination of tax abuses in international business. It were the EC decisions that inspired several Member States to adjust their law, without waiting for the final ECJ judgement to follow.

The numerous EC decisions, eliminate any signs of anticompetitive instruments from the internal market. The EC point of view, exposed in the Notice on the state aid notion, is therefore expected to be confirmed by the ECJ judgements, once the cases (regarding tax rulings or selective advantages) still in progress, will be closed. Its brings to the conclusion that it is the European Commission who has the most influence on the Member States legislation with regard to competition in taxation.

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Subsidy in the Light of the Law of the European Union

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Abstract

Subsidies are granted by the authorities of third countries and constitute a financial support of a domestic entrepreneur of that country. Public funds granted to entrepreneurs allow them to reduce prices and to compete much more easily on foreign markets, and for this reason subsidies are often regarded as unfair competition. A subsidy has been defined in the Regulation 2016/1037. The recognition of a subsidy subject to countervailing measures provides for three conditions: the financial contribution, the advantage and the specificity of the subsidy. In order for the countervailing measures to be imposed, four requirements should be met: the existence of a subsidy which is subject to countervailing measures; the existence of injury to the Union industry; a causal link between the subsidy and the injury and the existence of the "European Union's interest". This article aims to present the issue of subsidies in international context and to analyze the notion of subsidy in the light of the law of the European Union. Research methods used are analysis and synthesis regarding conclusion.

Keywords: Subsidy; Anti-Subsidy Proceedings.

JEL Classification: F13; F19; G18; H27; K33; P45.

1 General considerations

According to Eriksson et al. (1998), financing mechanism used to generate subsidy flows may seriously erode the effectiveness subsidy policies.

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Anti-subsidy procedure is closely connected with a specific financial supply under the name of subsidies (Drwiłło, 2003). They constitute an instrument of commercial policy affecting the structure of the economy of many countries, including those that make up the European Union. Their occurrence triggers specific reactions from the European Union, on whose territory subsidized goods occur. Subsidies are a kind of public aid aimed at supporting entrepreneurs. They are granted by the authorities of third countries and constitute a financial support of a domestic entrepreneur of that country. This is a non-returnable financial assistance provided by government authorities.

It is worth paying attention to the similarity and relationship of such concepts as subsidy and subvention; according to Polish law the latter is also a form of financial assistance granted by public authorities to specific entities. Initially, these concepts were not distinguished. Later the legislators gave these concepts a strictly defined meaning. There is a need to distinguish these concepts despite the existence of certain similarities. Another type of non-repayable financial assistance provided by the government is a donation in the meaning of Polish law. It is a free and non-returnable (with some exceptions) cash benefit granted by the state to various organizational units. It aims to implement public tasks through these organizational units. Donations can be directed to a wide range of entities (public and private). They serve to achieve a specific goal. Nowadays, it is not justified to substitute such terms as subsidy, subvention and donation. It is necessary to distinguish them on a normative basis.

The notion of free trade in relations with other countries is not without significance when considering subsidies (Rynarzewski, 2006: 263). The liberalization of international trade in goods is extremely valuable. However, its use in its pure form is not applicable. The liberalization of international trade relations is usually interwoven with the application of various constraints on these relations. There is also protectionism of international trade policy to a varying extent. The use of instruments of protectionist trade policy is characteristic especially for periods of deteriorating global economic situation.

The benefits of free international trade are undeniable. These are both economic and non-economic benefits. As a result of the international free trade policy, international specialization appears with good results, which improves the efficiency of production processes, reduces unit production

costs, increases consumption as a result of lower prices of imported goods and stimulates capital investments. Such phenomena should be included in economic benefits. Non-economic phenomena include, among others, encouraging entrepreneurship, increasing employee responsibility and triggering their greater diligence. A noticeable benefit of free international trade is also the approximation of states as public organizations and closer contacts between citizens of different countries. The implementation of the idea of free international trade also promotes care for education, raising qualifications and mastering foreign language learning.

In international trade there is also a phenomenon of protectionism. There is no doubt that as a result of the protectionist policy, the state that uses it protects the domestic market (Michałek, 2002: 47). Such activities are aimed at maintaining domestic production at a certain level and limiting the phenomenon of unemployment. The use of instruments restricting the import of goods is also considered an activity that restores balance in the trade balance. One of the arguments for applying a protectionist policy is also the intention to oppose international trade competition. In some countries, the production costs (wages) are relatively low. As a result, companies producing goods in these countries are able to sell these goods at competitive prices on international markets; this phenomenon cannot be considered as unfair competition in international trade.

In general considerations on international trade, the transnational character of this trade cannot be overlooked. Within the framework of international trade, one should notice the existence of uniform goals and instruments as well as the phenomenon of harmonization and coordination in various territorial levels (countries, geographic regions). It should be noted that the main goal of the supranational policy of international trade is to increase the well-being of societies belonging to a specific group of countries (for example to the European Union) or a geographical region. International organizations dealing with international trade operate on the world market. These include the General Agreement on Tariffs and Trade, the International Monetary Fund, the International Bank for Reconstruction and Development (World Bank) and the World Trade Organization.

Subsidies in international trade are a non-returnable cash benefit; their source is public money (Drwiłło, 2007). They serve the implementation of public tasks or other tasks, the financing of which is considered to be expedient. Sometimes their goal is to increase exports and thus improve the trade balance or reduce the surplus of produced goods in the country. One of the purposes of subsidies is the desire to improve the financial situation of producers (producers) of a particular good.

The transfer of funds in the form of government subsidies can be twofold: 1. direct, i.e. a non-returnable cash payment that equalizes the difference between the (lower) world price of exported goods and the (higher) national price, 2. indirect, i.e. the grant of a tax credit, refund of duty or application of a low-interest bank loan. It is worth noting that subsidies are not considered an optimal legal and financial instrument in terms of increasing the production of a particular good (Budnikowski, 2000: 240). The supplements for additional production are considered more favourable in this respect. Such supplements applicable to exported goods may be considered as export subsidies and subject to specific restrictions of applicable law.

An important consequence of the application of export subsidies is the reduction of world prices of the sold goods. As a result, the benefits achieved by the final purchasers of subsidized goods, i.e. consumers can be recognized. This however does not mean that the export subsidies are a fully desirable and accepted legal and financial instrument, as the disadvantages of using export subsidies should also be noticed. In fact, these shortcomings often determined the introduction and application of legal provisions limiting the use of export subsidies. Cheaper goods imported from other countries often have a destructive impact on the production and domestic sales of similar goods. Cheaper goods from other countries may limit the possibility of selling domestic goods. As a result, export subsidies are considered, though not always, as unfair competition practices. Export subsidies on one hand artificially stimulate exports, and on the other displace goods produced in the country from the market. In general, it can be assumed that export subsidies are in many cases a financial instrument supporting domestic producers by public authorities with clear signs of unfair competition on international markets.

2 Countervailable subsidies

The European Union is a member of the World Trade Organization; hence it is bound by the provisions of the SCM Agreement on Subsidies and Countervailing Measures during anti-subsidy proceedings. As a consequence, EU regulations on anti-subsidy proceedings should be in line with the SCM Agreement.

Regulation (EU) 2016/1037 of the European Parliament and of the Council of 8 June 2016 on protection against subsidised imports from countries not members of the European Union (OJ 2016 L176/55) defines the concept of subsidy. According to art. 3 it is considered that the subsidy exists if the public authorities of the country of origin or export have made a financial contribution or any form of income or price support within the meaning of art. XVI GATT from 1994 and in this way the benefit is granted. In addition, subsidies are subject to countervailing measures only if they are specific subsidies referred to in paragraph 2, 3 and 4 of the Regulation.

Thus, the recognition of a subsidy subject to countervailing measures provides for three conditions: the financial contribution, the advantage and the specificity of the subsidy.

There is a financial contribution by a government in the country of origin or export, where:

- a government practice involves a direct transfer of funds (for example grants, loans, equity infusion), potential direct transfer of funds or liabilities (for example loan guarantees);
- a government revenue that is otherwise due is forgone or not collected (for example fiscal incentives such as tax credits);
- a government provides goods or services other than general infrastructure or purchases goods;
- a government makes payments to a funding mechanism or entrusts or directs a private body to carry out one or more of the type of functions illustrated above which would normally be vested in the government, and the practice, in no real sense, differs from practices normally followed by governments.

The second requirement for a subsidy to be established is that the beneficiary of the subsidy has obtained the benefit. Sometimes the benefit is evident, for example if there has been a direct transfer of cash – in such a case, the value of the benefit is the sum of the funds transferred. Similarly, in the case of tax exemption, the value of the benefit is the value of the tax that has not been collected. In other situations, it is much more difficult to determine the benefit. For example, if the entrepreneur receives a loan from a state (state bank), it will require determining not only the conditions under which it was granted, but also the conditions under which loans are granted by commercial banks in similar situations (for the same loan amount and the same period of its repayment).

To prove the existence of a subsidy, it is extremely important to prove that the advantage has been achieved by exporters. Sometimes it can be stated that the benefit occurred, but it was received by entities other than exporters. For example, in the PET Film case (Polyethylene terepthalate (PET) film from India, OJ 1999 L 316/1) it has been proven that the beneficiary was the buyer of the goods and not the seller and for this reason it was considered that the advantage was not achieved by the exporters. In addition, when determining the occurrence of an advantage, the actual benefit achieved by the trader and not only the potential benefit is considered.

Subsidies are subject to countervailing measures only if they are specific subsidies. The concept of specific subsidies is set out in paragraph 2, 3 and 4 of the Regulation. This is due to the need to limit the potentially unlimited number of subsidies to those that actually impede competition as a result of selective support for specific industries or individual entrepreneurs (van Bael, Bellis, 2011).

3 Prohibited and specific subsidies

In the Regulation, the subsidy has been divided into two types: prohibited subsidies (Article 4(4)) and subsidies that are specific to certain enterprises (Article 4(2) and Article 4(3) of the Regulation 2016/1037).

Prohibited subsidies are treated as special subsidies, irrespective of whether they are or are not limited to individual enterprises. Prohibited subsidies are:

- subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I; subsidies shall be considered to be contingent in fact upon export performance when the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is accorded to enterprises which export shall not, for that reason alone, be considered to be an export subsidy within the meaning of this provision.
- subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods.

Annex I to the Regulation 2016/1037 contains an example of a list of twelve prohibited export subsidies. This list includes:

- the provision by governments of direct subsidies to a firm or an industry contingent upon export performance;
- currency retention schemes or any similar practices which involve a bonus on exports.
- internal transport and freight charges on export shipments, provided or mandated by governments, on terms more favourable than for domestic shipments;
- the provision by governments or their agencies either directly or indirectly through government-mandated schemes, of imported of domestic products or services for use in the production of exported goods, on terms or conditions more favourable than for provision of like or directly competitive products or services for use in production of goods for domestic consumption, if (in the case of products) such terms or conditions are more favourable than those commercially available on world markets to their exporters;
- the full or partial exemption, remission, or deferral specifically related to exports, of direct taxes or social welfare charges paid or payable by industrial or commercial enterprises;
- the allowance of special deductions directly related to exports or export performance, over and above those granted in respect

of production for domestic consumption, in the calculation of the base on which direct taxes are charged;

- the exemption or remission, in respect of the production and distribution of exported products, of indirect taxes in excess of those levied in respect of the production and distribution of like products when sold for domestic consumption;
- the exemption, remission or deferral of prior-stage cumulative indirect taxes on goods or services used in the production of exported products in excess of the exemption, remission or deferral of like prior-stage cumulative indirect taxes on goods or services used in the production of like products when sold for domestic consumption; provided, however, that prior-stage cumulative indirect taxes may be exempted, remitted or deferred on like prior-stage cumulative indirect taxes may be exempted, remitted or deferred on exported products even when not exempted, remitted or deferred on like products when sold for domestic consumption, if the prior-stage cumulative indirect taxes are levied on inputs that are consumed in the production of the exported product (making normal allowance for waste);
- the remission or drawback of import charges in excess of those levied on imported inputs that are consumed in the production of the exported product (making normal allowance for waste); provided, however, that in particular cases a firm may use a quantity of home market inputs equal to, and having the same quality and characteristics as, the imported inputs as a substitute for them in order to benefit from this provision if the import and the corresponding export operations both occur within a reasonable time period, not to exceed two years;
- the provision by governments (or special institutions controlled by governments) of export credit guarantee or insurance programmes, of insurance or guarantee programmes against increases in the cost of exported products or of exchange risk programmes, at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes;
- the grant by governments (or special institutions controlled by and/or acting under the authority of governments) of export credits at rates below those which they actually have to pay for the funds so employed

(or would have to pay if they borrowed on international capital markets in order to obtain funds of the same maturity and other credit terms and denominated in the same currency as the export credit), or the payment by them of all or part of the costs incurred by exporters or financial institutions in obtaining credits, in so far as they are used to secure a material advantage in the field of export credit terms;

- any other charge on the public account constituting an export subsidy in the sense of Article XVI of the GATT 1994.

Domestic subsidies other than export subsidies will be subject to countervailing measures only if they are specific subsidies. The literature emphasizes that public authorities have the right to subsidize entrepreneurs, provided that they do not favour any of the industries. Because of this, so-called horizontal subsidies are not classified as specific and subsidies limited to specific enterprises or industries are considered special and may be subject to countervailing measures (van Bael, Bellis, 2011).

Three principles are applied to determine whether subsidies are specific. The first two concern the so-called de jure specificity, i.e. the situation where the subsidy is legally dependent on export activity, while the third rule concerns the so-called de facto specificity, i.e. the situation where the subsidy method indicates that the subsidy is limited to individual market participants.

According to the first principle, defined in Article 4 item 2a of the Regulation 2016/1037, where the granting authority or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific. I. van Bael and J. F. Bellis point an example when the subsidy program is clearly limited to strictly identified market participants, for example ‚company x' or ‚carpet manufacturers' (van Bael, Bellis, 2011).

The second rule sets a negative premise. Where the granting authority or legislation pursuant to which the granting authority operates establishes objective criteria or conditions governing the eligibility for, and the amount of, a subsidy, specificity shall not exist, provided that the eligibility is automatic and that such criteria and conditions are strictly adhered to. Objective criteria or conditions means criteria and conditions which are neutral, which do not favour certain enterprises over others, and which are economic in nature and

horizontal in application, such as number of employees or the size of the enterprise. These criteria or conditions must be clearly set out by law, regulation or other official document, so as to be capable of verification.

According to the third principle, if, notwithstanding any appearance of non-specificity resulting from the application of the first and second principles, there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. Such factors are: use of a subsidy programme by a limited number of certain enterprises; the granting of disproportionately large amounts of subsidy to certain enterprises; the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy. In this regard, information on the frequency with which applications for a subsidy are refused or approved and the reasons for such decisions shall, in particular, be considered.

Subsidies which are not specific subsidies in accordance with Article 4 are not subject to countervailing measures.

4 Requirements for the imposition of compensatory measures

It should be emphasized that the mere statement that a subsidy is a countervailable subsidy is not sufficient to impose compensatory measures. In order for the countervailing measures to be imposed, four requirements should be met:

- the existence of a subsidy which is subject to countervailing measures;
- the existence of injury to the Union industry;
- causal link between the subsidy and the injury;
- the existence of the "European Union's interest".

Injury means material injury to the Union industry, the threat of material injury to the Union industry or a material retardation of the establishment of such an industry. The determination of injury shall be based on positive evidence and shall involve an objective examination of the volume of subsidized imports and the effect of the subsidized imports on prices in the Union market for like products and the consequent impact of those imports on the Union industry.

The third requirement, which should be fulfilled in order to impose countervailing measures, is to demonstrate the causal link between the subsidized imports and the injury. The research also covers factors other than imports of subsidized prices, which are detrimental to the Union industry. This is done to ensure that the damage caused by these factors cannot be attributed to the subsidized imports.

A determination as to whether the Union's interest calls for intervention shall be based on the appraisal of all the various interests taken as a whole, including the interests of the domestic industry as well as users and consumers. This determination shall be made only where all parties have been given the opportunity to make their views known. In such an examination, the need to eliminate the trade-distorting effects of injurious subsidisation and to restore effective competition shall be given special consideration.

Measures, as determined on the basis of subsidisation and injury found, may not be applied, where the authorities, on the basis of all the information submitted, can clearly conclude that it is not in the Union's interest to apply such measures.

5 Conclusion

Subsidies are a kind of public aid aimed at supporting entrepreneurs. This assistance may be of direct nature, for example in the form of a non-returnable cash benefit or indirect, as exemplified by the granting of a tax credit, duty drawback or the use of a low-interest bank loan. Public funds granted to entrepreneurs allow them to reduce prices and to compete much more easily on foreign markets, and for this reason subsidies are often regarded as unfair competition. It should be pointed out that not all subsidies are reprehensible, but only those that have a negative effect on international trade.

For this reason, the adoption of the normative definition of a subsidy in Regulation 2016/1037 deserves recognition. The preconditions for a subsidy to be considered as a subsidy are the financial contribution or income support by the government or any public institution, the beneficiary's benefits and the specificity of the subsidy.

COUNCIL REGULATION (EC) No 2026/97 of 6 October 1997 on protection against subsidized imports from countries not members of the European Community

The adoption of the definition of subsidy made it possible to provide a clear and predictable legal framework for traders making international transactions. However, the lack of regulation of non-countervailing subsidies should be criticized. Until 2002, the provisions of the previous Council Regulation (EC) No 2026/97 of 6 October 1997 on protection against subsidized imports from countries not members of the European Community (OJ 1997 L288/1) indicated examples of subsidies not subject to countervailing measures, in particular the so-called green list of subsidies not countervailed under the provisions of the SCM Agreement of the World Trade Organization. In accordance with the provisions in force at that time, the countervailing measures did not cover subsidies that were not specific, as well as subsidies, which were admittedly specific but met the conditions laid down in paragraph 1, 2, 3 or 4 of article 4 of Regulation 2026/97 (i.e. the so-called green subsidies, for example subsidies for research, aid for disadvantaged regions, subsidies to support the adaptation of existing facilities to new environmental requirements, and the subsidy component). It may have occurred in any of the measures listed in Annex IV (the so-called green box). The relevant WTO regulations expired on 31 December 1999, and as a result of Council Regulation 1973/2012 (OJ 2002, L305/4), the provisions of the then binding anti-subsidy Regulation 2026/97 were repealed. In cases initiated after this period, these green subsidies have been considered countervailable. De lege ferenda, it is necessary to propose legal regulation of the issue of non-countervailable subsidies.

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Public Finance and Financial Assistance Funds

Petr Mrkývka[1], *Johan Schweigl*[2]

Abstract

There have been numerous significant measures taken within both the monetary and fiscal areas of EU economic policies when the EU and national authorities were taking steps towards stabilisation of sustainability of public finance of some of the EU member states. In this paper, the authors focused on both the theoretical and practical aspects of the financial assistance (rescue) funds and mechanisms, which have been established by the EU member states or directly by the EU over the last decade. A special emphasis is given to the European Monetary Fund that is being shaped at the moment. Aside from the practical issues, the authors also focused on certain issues of the theory of financial law and public finance.

Keywords: Financial Assistance Funds; Public Finance; Sovereign Debt; European Monetary Fund; European Stability Mechanism.

JEL Classification: K40; H12; H63.

1 Introduction

'Public finance' is a term that is often used in social sciences. It mainly covers the area of economics and law. A number of authors have tried to present a perfect definition of 'public finance'; with more or less success.

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Almost each book on macroeconomics or 'classic' financial law contains its author's view of public finance. As Eugeniusz Ruśkowski aptly stated, "*public finance is a complex and dynamic phenomenon.*" (Ruśkowski, 2018)

Public finance is a part of a category relating to public financial activities of the state, i.e. direct or indirect managing of money by the state or the bodies of public administration. From the view of economics, public finance are means that the public sector has for carrying out its functions, or to be more precise, the tasks assigned to it by means of political decisions and laws. From the perspective of sociology and law, public finance rather covers very specific social relationships connected with public financial activities. These relationships and the behaviour of its subjects are viewed as the 'object of interest' of the public financial policy and also the 'object' of regulation by the financial law.

Public financial policy is a mainly a policy of the state, of the government. Aside from the state, also public self-administration and the EU have their own financial policies. Financial policy of the EU is formed within very complex processes trying to find harmony among the political formations, particular member states and the EU as a whole. Regardless of the maker of the policy, the role of law in the realm of financial policy is twofold; it is a tool for its implementation and also its border line.

In general, public financial policy is a financial strategy for ensuring material foundation for carrying out the functions of an entity (union, state or other public corporation). As the financial policy is rather of complementary nature, it serves other segments of policies of the entities. Origination of the financial policy and definition of its goals are carried out together with other policies and their goals.

The 'complementarity' of financial policy does not mean that it would be subordinate to other political goals. These other goals have to comply with the needs of the financial policy, such as price stability, stable financial sector, budget strategy, etc. As for the states of the Central and Eastern Europe (regardless of the EU membership), the role of financial policy within the area of public policy, has been shaped by the long-term transformation of economy from the model of centrally planned economy to market economy, i.e. from government direction to economy based on principles

of free trade and minimal direct intervention into the economic live of the society. This evolution in the approach and meaning of the financial policy has also been reflected in the development of financial law. The economic transformation of Bulgaria, Czech Republic, Estonia, Croatia, Lithuania, Latvia, Hungary, Poland, Romania, Slovakia and Slovenia, together with the overall process of democratisation of society has been connected with European integration. In early 1990s, these countries of the former Eastern Bloc had set a goal to become a part of the European integration. This became reality 15 years ago.

Such a step was crucial; huge effort was made when adjusting the political, legal and technical standards with the western European democracies. The rather naive fantasy of quick wiping off of the differences between the East and the West of Europe had to deal with some unexceptional problems – economic recessions, crises of public finance, financial crisis and migration crisis. The cultural differences between the new and the old democracies have been obvious and not even fifteen years of being members of the union did not lead to acceptance of common values, loyalty to the principles of the EU and mutual solidarity. All this led to an increase of scepticism or even aversion to the existing form of European integration, often supported by political ambition of some parties from both sides of the political spectrum. National egoism supported also by foreign means has become the hindrance of improvement of the European integration. This crisis of common Europe has also reflected in the Czech Republic, mainly by rejecting the Constitution for Europe, Fiscal Pact and rather political scepticism towards the common currency and banking union(Blažek, Schweigl, 2019). We can now witness a very specific situation, in which the economically weaker member states accept the EU and the integration better than the states with much higher economic potential, e.g. the Baltic countries, which all joined euro and Bulgaria, which strives to join it. Similar approaches may be identified in Croatia.

So far, we defined public financial activities as the activities of the state and public administration (mainly territorial administration). Public financial policy and public administration has been similarly understood as connected to a particular state or local entities within the concept of fiscal federalism.

If we leave the political and economic aspects aside and focus only on the legal nature, we may say that:

- The EU member states transferred upon its free decision part of its sovereignty on the EU. These states did not waive its sovereignty in favour of any other state, but they rather included it as their own share in the financial sovereignty of the specific form international integration entity. This means that a member state is empowered to take part in making decision about financial sovereignty of the Union and its realisation.[3]
- Public financial activity shall be understood as direct or indirect managing of money (Mrkývka, 2012: 49), within the own and joint financial sovereignty, carried out not only by the state and its bodies and public self-administration authorities, but also by the EU. The European financial activity may be viewed as a collection of financial activities of the member states and the EU as a single entity. As such, it is a complex set of activities, in which the differences of the EU bodies and the bodies of the member states must be considered. We shall also distinguish between the states with higher form of financial integration (mainly the eurozone members) and the states with minimal financial integration, such as Poland, Czech Republic or Hungary. Even here, we should focus on how much their independent financial activity influences the realisation of financial policy of the Union.
- With respect to the very specific nature of the EU, which is neither a classic international organisation, or (so far) any super-state, and in light of the fact that even an individual may be affected by the broadly defined public financial activities, these relationships are not only international (inter-states) relationships. This creates a very special category of finance with a specific regulation. This also corresponds with the unique legal form of the EU.

Public financial activity, as a collection of activities more or less connected with direct and/or indirect managing of money follows one unifying postulate – sustainable development. As for the EU, this may be viewed as a general expression of all the postulates included in the preamble of the Treaty

3 Compare the art. 5 of the Treaty on Functioning of the EU, as amended by the Lisbon treaty.

on the EU. Legislation which regulates the public financial activities in the EU (European financial law) contains of:

- The laws of primary EU law;
- Directly applicable laws of the Union law which regulates the financial activities of the bodies and institutions of the EU;
- Directly applicable laws within the entire territory of the EU;
- Laws directly applicable in the eurozone countries;
- Directives and national laws of the particular member states in which the directives were implemented;
- Other laws regulating public financial activities in the particular member states, including the normative administrative acts of public administration.

European financial law is, similarly to the Czech national financial law, an internally differentiated branch-unit fulfilling the unifying postulate, which is more or less laid down in the art. 3 item 1 of the Treaty on Functioning of the EU: "*The Union's aim is to promote peace, its values and the well-being of its peoples.*" Viewing European financial law as a branch-unit may be in the form of formal acceptance by the legal theory. Here, however, the overwhelming national approach to systematisation of law would prevail. Nevertheless, we may expect factual recognition of European financial law, mainly in legislation and legal practice – in a single approach to regulation of public financial activity.

If we view public financial activity as a financial activity of the Union, the member states and their public corporations, including their managing of money, these activities can be carried out either directly or indirectly. These activities may be either relating to certain funds or be of monetary nature. In such a public administration of money, it is important, regardless of the nature of such activities, to observe the principle of financial harmony. This principle arises from a pathological cognition that a cause of a negative state in one segment of financial activities may be in a negative behaviour or state of one of the other segments. Interconnection between the fund-related and monetary activities is obvious in critical moments when instability of currency also destabilises certain monetary funds, and, on the other hand, a public finance crisis may destabilise currency. The cause

of certain negative phenomena of a particular segment may thus have roots in wrong decisions made in another segment. Hence, it is always important to observe the secondary influence of the decisions made in one segment on the other segments. Direct or indirect managing of money requires specific approach; thus the use of respective instruments of the applied method or regulation. (Kyncl, Mrkývka, Bárta, et al., 2013).

For considering the nature of financial activities of the EU and its member states and the respective relationships including the regulation, we shall further aim at the financial activity of the EU in the area of the financial assistance funds.

2 The Path to New Financial Assistance Funds

The year of 2009 meant not only a 10 year anniversary of creation of euro, as a single currency of the euro area countries, but it was also a year in which it became more than clear that certain regulatory measures need to be taken in order to deal with the fiscal challenges of some the euro area countries. In 2010, some of the advanced countries within the euro areas averaged a budget deficit of 8,3 % and the public debt to gross domestic product ratio in those economies reached a level of 97 %, increasing from below 75 % in 2006 (Olivares-Caminal, 2011). Not only the European banking sector, due to its (both direct and/or indirect) exposure to the US subprime market, dealt with the consequences of the financial crisis of 2008, but it started to feel the pressure of raising yields on the sovereign bonds issued by some of the euro area member states. The EU authorities had to take measures to keep the banking sector viable, give certain incentives to slowing economy, support malfunctioning transmission mechanism, etc.

Despite the fact that there were numerous steps taken at a number of levels, there are two core areas in which some of the key actions were taken: (i) the area of monetary policy and (ii) the fiscal policy. Nonetheless, some of these steps may show signs of both the monetary and fiscal incentives.

In this paper, we will focus solely on the fiscal area, namely on creation of so-called financial assistance funds, or rescue funds. A special emphasis will be placed on the fund that is currently being shaped, i.e. the European

monetary fund (EMF). The goal of this paper is twofold. Using the historical perspective, we will outline the complicated and not always very systematic journey, which lead from the rather *ad hoc* created funds to the currently planned EMF. Second, the rescue funds will be considered from the perspective of the financial law theory (Mrkývka, 2008), since these funds have rather been ignored by the legal theory despite their huge impact on both the legal practise of public finance and the connected importance for the theory of public finance.

3 Responses to Sovereign Debt Crisis in the EU

In early 2010, it was obvious that monetary policy measures represented mainly by the Securities Markets Programme (SMP), which had been announced by the Governing Council of the European Central Bank (ECB) on 10 May 2010, would not suffice. The goal of SMP was to ensure depth and liquidity in malfunctioning segments of the debt securities markets and to restore an appropriate functioning of the monetary policy transmission mechanism, but the use of monetary policy tools has it limits.[4] Some of these limits have been laid down even in the establishing EU treaties,[5] other limits are rather of objective nature – although monetary policy plays an important role in combating economic slowdowns it does not have an unlimited power. Nonetheless, their advantage is that they may be applied very fast. It is common that central banks have the authority to use their tools upon the decision of their core body – as for the ECB, the most important decision-making body is the Governing council.

Fiscal policy steps usually take more time to be carried out, as they require the legislative and/or executive authority to act. At the EU level, there were several measures of rather fiscal nature taken. Establishment of so-called 'financial assistance funds' or 'rescue funds' belongs to those having far-reaching effects. Some of these funds were established within the legal

4 Comp. for instance, the Monthly bulletin of ECB, May 2010. Available at: https://www.ecb.europa.eu/pub/pdf/mobu/mb201005en.pdf

5 For instance, see the art. 123 of the Treaty on the Functioning of the EU (TFEU), which bans the central banks of the EU member states and the ECB, i.e. all the members of the European system of central banks (ESCB) to monetise public debt, in other words to directly extend credit to public institutions.

framework of the EU, others out of the framework. Some had been shaped to be rather temporary, whereas others were designed as permanent funds. Below, we outline the particular funds.

In early 2010, there was a comprehensive package of fiscal measures decided. First the Hellenic Republic was given a direct stability support loans by the euro area member states and later the European Financial Stabilisation Mechanism (EFSM) was created. EFSM was established within the framework of the EU law, by means of a council regulation. The EFSM was used to provide financial assistance conditional on the implementation of certain austerity measures to Ireland and Portugal and also for providing a bridge loan to the Hellenic Republic.

The assistance provided to Ireland was made in the joint force of the EU and the International Monetary Fund (IMF). Although Ireland no longer receives any support, it shall remain subject to post-programme surveillance until at least 75 per cent of the assistance is fully paid off. Portugal is now also subject to such surveillance. EFSM's creation is based on the art. 122 of the Treaty on the functioning of the EU (TFEU), which makes it possible for the council, upon a proposal of the European Commission to "decide, in a spirit of solidarity between Member States, upon the measures appropriate to the economic situation, in particular if severe difficulties arise in the supply of certain products, notably in the area of energy." EFSM thus emerged based on a legislative act. It is a mechanism, not a legal entity. From this perspective, EFSM may be considered as a public-law mechanism established by an act of secondary EU law.

Following the EFSM, there was established the European Financial Stability Facility (EFSF). This fund has been created out of the scope of the EU law, as a société anonyme incorporated in Luxembourg on 7 June 2010. The function of the fund including the condition of the financial assistance have been laid down in EFSF Framework Agreement, which was concluded by Belgium, Germany, Estonia, Ireland, Hellenic Republic, Spain, France, Italy, Cyprus, Luxembourg, Malta, Netherlands, Austria, Portugal Slovenia, Slovak Republic, and Finland, which are the EFSF shareholders on the one side, and the EFSF, on the other. In other words, the newly established corporation (société anonyme) entered into a contract with its shareholders,

i.e. with the EU member states who adapted euro as their currency. It might seem unclear whether or not EFSF is of private or public law nature. Its shareholders are only states, but it has been established as a private law entity, a corporation. Even a provision of financial assistance from this fond is regulated by a private law instrument – by a contract. Despite the fact that its purpose is clearly serving a public interest, the structure and origination of the EFSF seems to be rather of private law nature (Schweigl, 2018).

The third in a row was the European Stability Mechanism (ESM). In spite of its title suggesting that it is again a mere mechanism, such as EFSM, the ESM is a legal entity having its legal capacity (legal personality). It has been established by the EU member states who adopted euro in form of an international treaty (Tichy, 2012). From this perspective, ESM may be viewed as an entity of public international law, an organization established based on an international treaty. As such, ESM was again established out of the scope of the EU legal framework. Although it had not been created by an act of the EU law, it is an organization who was set up by (some of the) EU member states based on empowerment to do so – under extraordinary circumstances – given to the establishers by the art. 122 of the TFEU. As opposed to the EFSM and EFSF, which were ad hoc funds, providing financial assistance for a particular purpose known even before their creation, ESM was established with an idea of having a permanent fund, which would help to counter even the possible future financial distress and prevent the risk of financial contagion. This ESM was set to closely cooperate with IMF in providing stability support. ESM was providing stability support to its members when regular access to market financing was impaired or at risk of being impaired. Nevertheless, as the fund was created out of the framework of the EU law, it was obvious that sooner or later there would become efforts to include it embody it into the EU law.

These efforts started to be discussed in a more complex way in late 2017. In 2018, a proposal of a regulation on creating European monetary fund (EMF) was introduced by the European Commission. This fund shall embrace and combine all some of the aspects of the EFSM and ESM. We may say that EMF enhances the risk sharing function of the previous ESM. This risk sharing function, however, "*must go hand-in-hand with the reduction of risk*

of sovereign and banking crisis" (Sapir, Schoenmaker, 2017: 4). Hence it is clear that a core creation of EMF would not suffice should the new introduced regulation of banking union legislative package would not be in place.

Aside from taking over the functions of the ESM, EMF should also work within the banking union's resolution mechanism as a common backstop. In other words, the single resolution mechanism is to be financed by contributions from the banking sector, not by the public funds obtained from taxpayers. If the single resolution mechanism lacks, however, the funds to carry out its functions, EMF should act as a backstop and lend the necessary funds to resolution mechanism. This function of the EMF is expected to avoid any turning of a banking crisis into sovereign crises when the sovereign cannot offer a credible backstop to its banking system (Sapir, Schoenmaker, 2017: 4).

To summarise, EMF should be created within the EU legal framework by means of a regulation, as such it would become an EU body with a legal personality, acting as a direct successor of ESM assuming all its rights and obligations. Thus, it should take over most of the functions from the ESM. In other words, an entity of international law with its functions (ESM) should be drawn into the legal framework of the EU. Such an integration would change the structure of democratic accountability, as the role of national parliaments would be curtailed to information rights (currently, some parliaments de facto have a veto right in the ESM's decision making framework) (Scheinert, 2019: 6).

The core objective, as such may be view as to making the financial sector of the EU more resilient and stable. EMF is expected to be established in 2019.

4 Conclusions

The financial assistance funds represent a very specific area of public financial activities. This area is generally researched by several sciences, mainly by economics and financial law. We have first shown the position and the role that financial assistance funds have within the system of public finance and within financial law regulation.

Having outlined the particular financial assistance funds of the last post-crisis decade, we focused mainly on the currently-being-shaped European Monetary Fund.

This fund is a typical example of interconnection between particular segments of public financial activities. It comprises both the budgetary (fiscal) and monetary aspects of public financial activities. As such, its structure, role, function and legal basis should be given more attention not only but the economists, but also by the experts in financial law.

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The Implementation of the Common Budgetary Timeline in the Member States in the Euro Area as Illustrated by the Example Of Italy

Przemysław Panfil[1]

Abstract

This article attempts to assess the regulations establishing the common budgetary timeline in the Euro area member states. It was introduced into the EU legal order in 2013. This instrument should be regarded as another attempt to strengthen the legal framework of coordinating the EU fiscal policies. Thus, it is part of a series of actions taken by the EU legislator influenced by the debt crisis experience. This paper is based on the research hypothesis according to which the common budgetary timeline increases the political costs of ignoring the budgetary policy requirements by the Euro area governments. A dogmatic analysis was applied during works on this publication.

Keywords: Euro Area; Stability And Growth Pact; Draft Budgetary Plan.

JEL Classification: G21; G23; G28.

1 Introduction

The European Commission (hereinafter: Commission) issued an opinion concerning the Italian draft budgetary project (European Commission: C(2018) 7510) on 23 October 2018. The Commission identified "a particularly serious non-compliance with the budgetary policy obligations laid down in The Stability and Growth Pact" and called on the Italian government to effect relevant changes as soon as possible. Thus, for the first time in history, the Commission exercised its powers under Article 7.2 of the Regulation (EU) No. 473/2013 of the European Parliament and of the Council

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of 21 May 2013 on common provisions for monitoring and assessing draft budgetary plans and ensuring the correction of excessive deficit of the Member States in the Euro area (hereinafter: Regulation No. 473/2013). This act introduces, inter alia, the common budgetary timeline for the members states in the Euro area. This institution can be regarded as another element of the multilateral surveillance exercised by the EU authorities over the public finance condition of the member states.

This article attempts to assess the regulations establishing the common budgetary timeline in the Euro area member states. The implementation of this objective requires identifying the premises for introducing this institution into the EU legal order, analysing the adopted legislative solutions and verifying how these measures work in practice. This paper is based on the research hypothesis according to which the common budgetary timeline increases the political costs of ignoring the budgetary policy requirements by the Euro area governments. A dogmatic analysis was applied during works on this publication. The article refers to the valid normative material, secondary sources in the available literature and the EU and Italian official documents.

2 Reasons for implementing the common budgetary timeline

While establishing the Euro area it was clear that it would not meet the conditions of the so-called optimal currency area in the foreseeable future. This increased the risk of abusing the fiscal policy by the Member States to stimulate economic processes. The related negative consequences for fiscal stability were perceived as a serious challenge for the process of the monetary integration in Europe. As a result, the need to establish the legal framework arose for coordinating the fiscal policy of the Euro area countries, and – to a slightly more limited extent – other members of the European Union. The provisions contained in the title of VIII Treaty on the Functioning of the European Union (hereinafter: Treaty) are crucial in this regard. In particular, they oblige all Member States to avoid the excessive deficit and create a framework of the so-called excessive deficit procedure. In this

way, the Treaty introduces the fiscal policy rules and mechanisms ensuring compliance with them into the EU legal order.

Quite general provisions of the Treaty are specified in the attached Protocol No. 12 and in the Council Regulation (EC) No. 479/2009 of 25 May 2009 on the application of the Protocol on the excessive deficit procedure annexed to the Treaty establishing the European Community. These acts set reference values concerning public debt and deficit and introduce legal definitions that shall be interpreted from the point of view of the provisions laid down in the Regulation (EU) No. 549/2013 of the European Parliament and of the Council of 21 May 2013 on the European system of national and regional accounts in the European Union.

The EU fiscal policy coordination system was additionally strengthened in 1997 when the three-element Stability and Growth Pact was established (hereinafter: Pact). The first element was the Resolution of the European Council of 17 June 1997 on the Stability and Growth Pact under which the Member States committed themselves to observe the medium-term budgetary objectives close to the balance or in surplus position. The second element was the Council Regulation (EC) No. 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (hereinafter: Regulation No. 1466/1997). This act comprises the so-called preventive arm of the Pact, implementing an early warning mechanism. The last one is the Council Regulation (EC) No. 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure. It complements the above-mentioned procedure and the system of sanctions imposed within its scope, thus creating the corrective arm of the Pact.

The first years of the operation of the legal framework concerning the Member States' fiscal policy coordination revealed numerous problems with their practical use. The lack of determination in implementing the medium-term budgetary objectives by the Member States became particularly clear. As a consequence, the first major modification of the Pact took place in 2005, which unfortunately did not basically improve its effectiveness. The scale of the issue manifested itself especially under the influence of the global financial crisis which led to a dramatic deterioration in public finances of the EU states and

the outbreak of the debt crisis in the Euro area. Importantly, in 2008–2010 the excessive deficit procedure was opened against 22 Member States (Panfil, 2017b: 114). In addition, several Euro area countries were on the brink of bankruptcy (Panfil, 2017a: 407). This clearly showed the low effectiveness of the Pact, especially its preventive arm. In case of the latter one, the problem appeared to be the key decision-making system under the early warning mechanism as well as the fact the system did not provide for the possibility of imposing sanctions on Member States. Thus, this mechanism could be regarded solely as a way of signalling the concern about the budgetary position development in a given country by the EU Commission and the Council (hereinafter: Council) (Panfil, 2017: 125).

The above-mentioned circumstances were premises for two major modifications of the legal framework for fiscal policy coordination of the EU Member States. They were implemented in 2011 (the so-called six-pack) and in 2013 (two-pack). One of the elements of the latter modification was the introduction of the common budgetary timeline for the Euro area member States under the Regulation No. 473/2013. At the basis of this institution was the conviction that a good public finance state is best ensured at the stage of creating draft budgetary plans. Mistakes committed at this time cannot always be corrected while implementing the budget during a later period. Therefore, draft plans should first rely on objective and realistic macroeconomic and budgetary forecasts. Secondly, they should comply with:

- numerical fiscal rules established at the national level,
- the framework for economic policy coordination in the context of the annual cycle of surveillance (the so-called European Semester) which includes general guidelines for the EU Member States issued by the European Commission and the Council at the beginning of the cycle (pursuant to Article 2a.3 of the Regulation No. 1466/1997),
- recommendations under the Pact,
- and, where appropriate:
- recommendations made in relation with the macroeconomic imbalance's procedure (pursuant to the provisions of the Regulation (EU) No. 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances),

- opinions on economic partnership programmes adopted by the Council (in accordance with Article 9.4 of the Regulation No. 473/2013).

3 The shape of the common budgetary timeline

Pursuant to Art. 4 of the Regulation No. 473/2013, the Euro area Member States are obliged to:

- publicly disclose their national medium-term fiscal plans not later than by 30 April every year (preferably until 15 April). These plans cover at least all information that should be included in the stability programmes developed pursuant to Art. 3 of the Regulation No. 1466/1997;
- publicly disclose the draft budgetary plan for the coming year for the central government and key budgetary draft plan parameters for all the remaining subsectors of the general government not later than by 15 October every year;
- adopt/establish and publicize budget for the central government along with the updated main budgetary parameters for the remaining subsectors of the general government not later than by 31 December every year. At the same, Member States implement temporary budgetary procedures that shall be applicable if – for objective reasons beyond the control of the government – the budget is not adopted, set or made public until 31 December.

The draft budgetary plan is drawn up in accordance with the requirements set out in Art. 3.3 of the Regulation No. 473/2013. It consists of the catalogue of obligatory elements of this draft plan. These include, for example:

- the objective concerning the balance of subsectors of the general government expressed as a percentage of Gross Domestic Product (GDP), broken down by sub-sector of general government;
- the projections (at unchanged policies) for expenditure and revenue as a percentage of GDP for the sector of the general government and their main components;
- the main assumptions about expected independent economic developments and important economic variables which are relevant to the achievement of the budgetary targets;

- the annex containing the methodology, economic models and assumptions as well as any other relevant parameters providing the basis for the budgetary forecasts and projections for the impact of aggregated budgetary activities on economic growth.

The regulations contained in Art. 4.4 of the Regulation No. 473/2013 are also noteworthy. According to this provision, national medium-term budgetary plans and draft budgetary plans must be based on independent macroeconomic forecasts. This term is understood as forecasts prepared or approved by independent bodies within the meaning of Art. 2.1a of the Regulation No. 473/2013. *De facto* this means that each Euro area Member State is obliged to establish the so-called fiscal institutions and entrust them with a significant role at the first stage of the budgetary procedure. Moreover, this entity, pursuant to Art. 5.1 of the Regulation No. 473/2013 must monitor the compliance with domestic numerical fiscal rules by a given country. In this respect, EU solutions underpin a certain trend to create fiscal institutions which was particularly remarkable in Europe during the debt crisis (Panfil, 2016: 304–305).

Member States shall submit their draft budgetary plans to the Commission and the Eurogroup by 15 December. The Commission shall adopt an opinion on this matter no later than 30 November. Where the Commission identifies particularly serious non-compliance with the budgetary policy obligations laid down in the Pact, it shall within two weeks from the submission of the draft budgetary plan, request a revised draft budgetary plan from the Member State concerned. This request provides rationales and shall be made public. The Member State shall comply with its obligation to submit the revised draft budgetary plan within three weeks of the issuance of the opinion. This draft plan shall be subject to re-assessment by the Commission. The body issues a new opinion on the revised draft budgetary plan within a maximum of three weeks from the date of submitting the document by the Member State. This opinion shall be made public and submitted to the Eurogroup.

Applicable regulations do not provide for any discipline in the Member States which have not complied with the Commission's opinion. Nevertheless, pursuant to Art. 12.1 of the Regulation No. 473/2013, the response of a given

state is taken into consideration by the EU bodies acting on the basis of the provisions regulating the excessive deficit procedure. Thus, the government which does not take into account the Commission's opinion when preparing the revised draft budgetary plan, shall not forget about the negative consequences of their decision.

4 The dispute between Italy and the Commission about the draft budgetary plan for 2019

Throughout the whole time of the Euro area operation, Italy has a serious problem stabilizing its fiscal situation. Consequently, only twice – in 1999 and 2007 – it managed to bring the deficit of the central government sector below 2 % of GDP (Table 1). At the same time, this country has the highest level of indebtedness in the European Union after Greece. In 2017, the central government debt in Italy was 131,2 % of GDP with the average for the Euro area at 86,8 % of GDP. The public finance state in this country led Italy to being the subject of an excessive deficit procedure twice. The first procedure was in 2005–2008 and the second one in 2009–2013.

Table 1: Balance and debt of the central government debt in Italy in 1999–2017 (% GDP)

Year	Balance	Debt
1999	-1,8	109,7
2000	-2,4	105,1
2001	-3,4	104,7
2002	-3,0	101,9
2003	-3,3	100,5
2004	-3,5	100,1
2005	-4,1	101,9
2006	-3,5	102,6
2007	-1,5	99,8
2008	-2,6	102,4
2009	-5,2	112,5
2010	-4,2	115,4
2011	-3,7	116,5
2012	-2,9	123,4
2013	-2,9	129,0
2014	-3,0	131,8
2015	-2,6	131,6
2016	-2,5	131,4
2017	-2,4	131,2

NOTICE! The years when Italy was in the excessive deficit procedure are marked in grey

Source: the Eurostat website: https://ec.europa.eu/eurostat

The last excessive deficit procedure for Italy was completed in June 2013. During the subsequent years, this country did not make any significant progress in the public finance reform. The deficit in the sectors of the general government remained at the limit values. The debt was twice as high as these levels. At the same time, Italy remained outside the legally defined path of debt reduction and the achievement of the medium-term budgetary objective. By the end of 2017, this did not result in negative steps of the Commission thanks to flexible provisions of the preventive arm of the Pact, specifically the structural reform clause, the investment clause, and the unusual event clause[2]. As a result, in 2015–2018, Italy could temporarily depart from the path of achievement of the medium-term budgetary objective at nearly 1,8 % of GDP (European Commission, COM(2018) 809: 13). Nevertheless, on 13 June 2018, this country became the addressee of the Council's recommendations issued as part of the European Semester. According to these recommendations in 2019, the nominal primary expenditure growth should not exceed 0,1 %. This was intended to lower the deficit by 0,6 % of GDP and speed up the pace of debt reduction.

Italy submitted to the Commission their draft budgetary plan on 16 October 2018[3] (Ministero dell'Economia e delle Finanze, 2018b). This draft plan assumed that the economic growth in Italy would be 1,5 % of GDP in 2019 whereas the deficit and debt of the general government sectors would reach 2,4 % and 130,0 % of GDP respectively.

These data were assessed by the Commission in its opinion of 23 October 2018. The authority firstly highlighted that macroeconomic data which are the basis for the draft budgetary plan had not been prepared by the fiscal institution[4], which was the obvious violation of Art. 4. 4. of the Regulation No. 473/2013. At the same time, the Commission concluded that the submitted draft plan did not meet the Council's recommendations of 13 June 2018 and deviated from the assumptions of the Italian stability programme of the same year. In accordance with this program in 2019, the deficit

2 They included the migration crisis and seismic activity.

3 Thus, the application was submitted one day following the deadline specified in Art. 6.1 of the Regulation No. 473/2013.

4 In Italy, the Parliamentary Budget Office serves as an independent authority ensuring macroeconomic forecasts.

of the Italian General Government sectors was expected to be 0,8 % of GDP, while the debt 124,8 % of GDP (Ministero dell'Economia e delle Finanze, 2018a). As a result, the Commission identified particularly serious non-compliance with the budgetary policy obligations laid down in the Pact and called on Italy to submit the revised draft budgetary plan.

Italy submitted its revised draft budgetary plan on 12 November 2018 (Ministero dell'Economia e delle Finanze, 2018c). Sadly enough, its main assumptions were not significantly modified. Consequently, the Commission questioned the macroeconomic and budgetary data stated there. In particular, as estimated by this authority, the economic growth in Italy was expected to amount to 1,2 % of GDP, while the deficit and debt of the General Government sectors was respectively 2,9 % and 131 % of GDP (European Commission, (2018) 528). Thus, the Commission in its opinion of 21 November 2019 (European Commission, (C) (2018) 8028) reiterated its conclusions identifying particularly serious non-compliance with the budgetary policy obligations. On the same day, the Commission, relying on Art. 126,3 of the Treaty, issued a report identifying the risk of an excessive deficit in Italy (European Commission, COM (2018) 809). This step can be considered as the commencement of the formal way to initiate the excessive deficit procedure. Eventually, the Italian Parliament succumbing to the increasing pressure from the European Union authorities, passed the budget for 2019 which significantly differed from the draft budgetary plan of 12 November 2018. In particular, it was based on the revised macroeconomic assumptions. At the same time, the expected general government deficit was reduced to 2 % of GDP.

5 Conclusions

The regulations restricting the freedom of fiscal policy by the EU Member States are a response to the phenomenon referred to in the relevant literature as the deficit bias. It results from the idea of representative democracy, where citizens with active rights to vote select persons who are to represent the interests of the collective sovereignty subject. It is assumed that based on their knowledge, experience and access to information, they will make better decisions than a single voter. In this sense, the representative

democracy assumes the presence of information asymmetry. Taking advantage of this situation, politicians can achieve their particular objectives instead of acting in the interest of entire society (Calmfors, 2011: 657). One of them is usually the maximization of the electoral result. Therefore, politicians can make certain decisions only because they are common (Masin, 2004: 1035). At the public finance level, this issue is further exacerbated by the fact that an average voter prefers instant usability than a usability that can be achieved in the future (Frederick, 2002: 352). What is more, he is not fully aware of the existence and role of long-term budgetary constraints (Buchanan, 1997: 133). Consequently, he creates a false picture of alternative options to choose being affected by the so-called fiscal illusions. These illusions can be also specially created by politicians through the manipulation of indicators that describe the current or planned public finance state. This is possible due to creative accounting or a rather flexible approach to macroeconomic forecasts concerning, inter alia, the pace of economic growth or inflation (Kopycińska, 2006: 86–87). From the point of view of politicians, an additional advantage of this type of actions is the possibility to "circumventing" the fiscal policy rules, which usually restrict the freedom of the government as to the way of pursuing this policy (Poterba, 1996: 9). This rules are the permanent constraint of fiscal policy, typically defined in terms of an indicator of overall fiscal performance (Zawadzka-Pąk, 2017: 109).

The issues described above justify the implementation of such institutional solutions whose main purpose would be to reduce the information asymmetry between people shaping fiscal policy and voters. This is possible by ensuring the latter ones a reliable and independent from the government, source of information about the public finance condition. This source should publicize indicators concerning both the macroeconomic and fiscal situation of the country concerned. In addition, it should publish opinions on the impact on the budgetary position of decisions taken by public authorities. Universal access to this type of information could decrease the freedom of the government to create fiscal illusions and could increase the political costs of such operations.

Looking for the best institutional solutions that would be a response to the fiscal illusions created by public authorities, one more problem should

be mentioned. Namely, the access of an average voter to information sources that are independent of the government. This shall be of both the formal and material character. As objective, independent and expert source of information can be considered such international organisations as: The International Monetary Fund, the World Bank and the Organisation for Economic Cooperation and Development. Nevertheless, the data or reports presented by these entities have limited impact reaching the hands of a small group of experts. A similar situation can be observed in case of credit ratings for countries, developed by leading rating agencies.

The common budgetary timeline of the Euro area Member States, established by Regulation No. 473/2013 should be regarded as an attempt to respond to these challenges. First, it contains specific requirements for the draft budgetary plan. In particular, it must rely on macroeconomic forecasts developed by an independent fiscal authority. This solution alone reduces the ability of creating fiscal illusions by politicians. In this way, the government loses the opportunity to formally achieve the numerical fiscal rules by the simple manipulation of macroeconomic indicators.

Regulation No. 473/2013 confers the Commission the power to assess the government's draft budgetary plan. The opinion being the result of this assessment, like the draft plan itself, is made public. Thus, documents are exchanged between the governments of the Member States and the Commission. Undeniably, it is usually not a subject with a large medial influence. Everything changes, however, when the provisions of Art. 6.2. of the Regulation No. 473/2013 are applicable. In this case, in its opinion the Commission identifies particularly serious non-compliance with the budgetary policy obligations laid down in the Pact and calls on the Member State concerned to submit the revised draft budgetary plan. This type of call, as illustrated by Italy, has a huge medial potential. At the same time, the government of a Member State faces a very difficult decision. On the one hand, it can follow the conclusions specified in the opinion of the Commission and adapt the draft budgetary plan to them. In this way, however, it admits *de facto* that the original version of the draft plan was clearly inconsistent with the EU budgetary policy obligations. On the other hand, the revised draft budgetary plan can only include cosmetic changes.

Unfortunately, the revised draft plan is subject to another assessment of the Commission, whereas the conclusions are publicized again. At the same time, the government of the Member State thus exposes itself to ongoing peculiar discussions with the EU authorities. Nevertheless, it will be held on the basis of the provisions governing the excessive deficit procedure including the whole set of sanctions provided for by these provisions.

The analysis of the solutions governing the common budgetary timeline leads to the conclusion that it is a preventive instrument that complements the system for fiscal policy coordination of the EU Member States. It drastically increases the political costs of ignoring the policy requirements under the Pact. Undoubtedly, this is a factor that must be taken into account by the government that conducts the fiscal policy in a given country. The excessive loosening of the policy motivated by the desire to maximize the election result may be counterproductive. A possible conflict with the Commission on the public forum, draws the attention of voters to the actual public finance condition and reduces the information asymmetry. As a consequence, the government finds it more difficult to create fiscal illusions. Moreover, as a result of the changes that affected the Pact in 2011 and 2013, the Member States of the Euro area have a much lower chance of winning sport with the Commission. The experience arising from the dispute between the Commission and Italy suggest a weak negotiating position of domestic fiscal bodies. They must consider the possibility of applying the excessive deficit procedure by the EU bodies including all sanctions provided for in it.

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Concept of the Financial Legal Act in Financial Law of the European Union

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Abstract

Financial legal acts functioning in the Union legal order are regulated by EU financial law, a relatively young field of science, and in particular the science of Polish financial law. Having regard to the EU legal order, as far as it is possible to talk about legal regulations concerning its public finance, inasmuch as, from the formal point of view, the concept of "the EU financial law" basically has not been established in the European doctrine, what does not exclude the possibility to separate such a field on the basis of certain criteria. Taking the above consideration into account, the aim of this paper is to prove the following hypotheses: firstly – despite not common usage of the EU financial law concept, such a field may be distinguished in the Union legal order; secondly – including the specificity and the subject of such law regulations, within its range will function financial legal acts which may be subjected to proper typology.

Keywords: Policy Coordination; EU Public Finance; Financial Law; Financial Act; Sources of Law; Primary Law; Secondary Law.

JEL Classification: E61; H0; K1; K100; K40.

1 Introduction

The division of the EU law into primary and secondary has been generally accepted in the EU law science. It was used when the Union functioned

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as a structure based on the three pillars[2], as well as currently, i.e. after the reform of the system introduced by the Lisbon Treaty. However, it should be noticed that distinguishing primary and secondary law is not the way to classify the sources of law in such terms as they are examined in the theory of law, e.g. in regulatory terms, i.e. sources as rules of binding law (regulatory terms) (Lang, Wróblewski, Zawadzki, 1986: 413–416). This division proves rather the existence of general hierarchy of legal acts and connected with it relation between such acts covered by the frameworks of both distinguished groups. Primary law is generally established by the Treaties (Founding and Accession), although not exclusively, which have the highest rank in the EU legal order. They constitute certain constitutional order of the EU, thus they make its constitutional law. In compliance with them should be secondary law (Lenaerts, VanNuffel, 2011: 817–820), which is characterised by a complexity of legal acts of different character, covered by law-making and law application spheres. Here especially appear the acts with not only such features as: common scope, Treaty basis, general and abstract content, but also containing more precise and individual character. Therefore, not all legal forms appearing in the secondary law may be regarded as sources of law in the theoretical-legal meaning.

Even brief analysis of the primary and secondary law allows to formulate the following conclusion: the Union legal order is characterised by a diversity of law-making forms as well as other legal acts which have different legal rank (legal character). Despite the fact that the Lisbon Treaty was in particular to simplify and increase structure transparency of the legal acts, it is still quite expanded and complicated to a certain degree.

In the Treaty on the functioning of the European Union (TFEU) (OJ C 202, 7. 6. 2016: 1–388) was directly made a categorisation of legal acts due to the type of legislative procedure during which they are adopted. Pursuant to Art. 289, legislative acts, established by legislative procedure (ordinary or special), are distinguished. The result is that all other law-making acts, i.e. adopted during other procedures – at least from the formal and literal

2 According to the Treaty on European Union three pillars of Union were: European Communities, common foreign and security policy and police and judicial cooperation in criminal matters.

point of view – will not have a legislative status and therefore in the doctrine of the Union law they are classified as non-legislative acts (Heartley, 2010: 108; Chalmers, Davies, Monti, 2010: 415; Lenaerts, Van Nuffel, 2011: 885). This term appears also in the Treaty provisions, however *expressis verbis* it is not indicated that such acts constitute the effect of non-legislative procedure (e.g. such acts described as "delegated acts" are referred to in Art. 290(1) TFEU). This does not mean that non-legislative acts, taking into account the character of norms constructed on their basis, will always significantly differ from legislative acts (Lenaerts, Van Nuffel, 2011: 645). The referred Art. 289 TFEU uses only one procedural criterion (Hartley, 2010: 108) and does not refer to the legal nature of legislative acts. The group of non-legislative acts is internally diversified. On the one hand, there are acts which by their legal character, in particular general and abstract content and direct Treaty basis, will be similar to legislative acts, especially the ones adopted during a special legislative procedure. On the other hand, Art. 290–291 TFEU establish the so-called executive acts – delegated acts and implemented acts, which are to make legislative acts more specific and are to implement their provisions.

In turn, on the basis of material (subject) criterion in Art. 288 TFEU three basic regulatory instruments (law-making forms) were distinguished, through which EU secondary law provisions are established, i.e. regulations, directives and decisions[3]. Each of these forms is classified both as a legislative act (regulation) as well as a non-legislative act (delegated regulations, implemented regulations), depending on the legislative procedure in which it was adopted (Lenaerts, Van Nuffel, 2011: 885). Although the referred provision of the Treaty regulates material features of regulations, directives and decisions, still full evaluation of their legal character should also include the type of their adoption procedure.

Presented tripartite division of acts under secondary law is not closed, i.e. it does not exhaust all law-making forms of the EU activity. Several other acts may be distinguished, such as: interinstitutional agreements, budgets, resolutions, declarations, guidelines, clarifications, communications, codes

3 Art. 288 TFEU also indicates recommendations and opinions which have no binding force.

of conduct or by-laws. Some of them have Treaty basis and some have been developed during the practice of the Union institution. In professional literature it is common to describe them as a collective term of *sui generis* acts (Horspool, Humphreys, 2010: 116–119), however this group is not uniform, so the analysis of the legal content of this type of acts should be individual in relation to each of them.

In the whole structure of the Union law-making forms function also acts with financial content, which the Author defined as a collective category of "financial legal acts" or interchangeably – "acts of financial law". This category may be distinguished due to the subject of regulation of a given act, which is EU public finance, and more precisely – its public financial management. Therefore, such act will belong to the scope of EU financial law, a relatively young field of science, in particular the science of Polish financial law. Having regard to the EU legal order, as far as it is possible to talk about legal regulations concerning its public finance, inasmuch as, from the formal point of view, the concept of "the EU financial law" basically has not been established in the European doctrine, what does not exclude the possibility to separate such a field on the basis of certain criteria.

On the other hand, broad acceptance of financial law as a separate field of law is in the countries of Central and Eastern Europe. In the doctrine of the Polish legal science it is commonly assumed that the subject of such law regulation is public financial management (activity), thus managing public finance (Ruśkowski, Stankiewicz, 1991: 29–31; Borodo, 2005: 26; Ruśkowski, 2015: 104) and what is important – tendencies of its further development are noticeable (Ruskowski: 2018: 39–40), including shifting towards international financial law, also covering financial management and financial market of the EU (Kosikowski, 2003: 39; Kosikowski, 2005: 68–69; Drwiłło, 2018: 74–137).

Having regard to the above preliminary considerations, the aim of this paper is mainly to propose a concept of the EU financial legal act. According to the Author, it is justified to put a hypothesis that the acts of such type, including their specificity and subject of regulation, may be distinguished in the whole EU legal order and their typology may be conducted. Moreover, financial legal acts will belong to the scope of EU financial law, a field of the Union

law not very common in the doctrine of law, at least from the formal point of view.

The following research problems will be used to prove the above hypotheses:

- what is the scope and how can be characterized EU financial law functioning within the Union legal order?
- what features are EU financial legal acts characterised by and in what way their typology may be made?

Conclusion resulting from the analysis of the indicated problems have been established on the basis of non-reactive (non-empirical) research methods, i.e. based on source literature and binding EU legal regulations.

2 EU financial law as a separate field in the legal order of the Union

2.1 The specificity of the EU economic policy as an element determining the scope of its financial law

There is no doubt that the EU conducts public financial management by implementing specific aims determined by the provisions of the Treaties. The manner of conducting such management will guide financial policy (will be its content) and in a broader scope – EU economic policy.

The instruments implementing every economic policy (including financial one) are, among others, established legal norms (Ruśkowski, 2000: 28). Therefore, the question about the scope (shape) of the EU financial law should be limited in the first place to the explanation of the essence of the Union economic policy.

Broadly understood EU economic policy indicates significant specificity in relations to classic understanding of economic policy of a state as well as it has a complex character. It results from the fact that, on the one hand, the Union as an independent international organisation having legal personality and own institutions, on the basis of public funds generated in, among others: annual general budget, makes certain financial moves (decisions). On the other hand, all Member States, by preparing national budgets and making legal and financial norms also implement own fiscal policies,

and in a broader scope – economic policies. However, these countries function is a specific economic and legal environment which is largely determined by the membership in the EU. This environment is impacted by general aims of the Union determined in Art. 3 of the Treaty on European Union (TEU) (OJ C 202, 7. 6. 2016: 13–388). In the economic sphere they are mainly concentrated on: 1) creating uniform internal market, implemented by the principles of free movement of goods, people, services and capital; 2) facilitating permanent development of Europe based on sustainable economic growth, prices stability, highly competitive social market economy; 3) monetary integration under economic and monetary union. Thereby, the Member States also become actors of the whole Union economic policy and this in turn exerts the need to coordinate actions.

Such need to coordinate actions in conducting the EU economic policy was indirectly created by the principle of conferral regulated in Art. 5 TEU. On its basis the Union is authorised to act exclusively within the limits of the competence granted to it by the Member States in the Treaties, necessary to achieve goals determined in these Treaties, e.g. in the mentioned Art. 3 TEU. However, competence not granted may only be used by the Member States. Even in the case of granted competence the Union does not have full freedom of taking initiatives excluding the Member States. Because from Art. 2 TFEU results the division of competence granted to the Union into excusive competence and shared competence. The latter is exercised jointly with the Member States. Additionally, the freedom of implementing the Union's actions on the basis of the principle of conferral was limited by resulting from it principles of: proportionality (Art 5(4) TEU) and subsidiarity (Art 5(3) TEU).

Forms of the EU economic policy coordination are indirectly determined by the referred principle of conferral as well as by distinguishing exclusive and shared competence in particular fields. The consequence of establishing the principle of conferral and specifying exclusive and shared competence in particular fields mentioned in Art. 3 and 4 TFEU are its other provisions which directly indicate the obligation to coordinate, i.e.:

- Art. 5 and Art. 120–121 – determining general obligation to coordinate economic policies of the Member States within the Council;

- Art. 119(1) TFEU – ordering to maintain strict coordination of economic policies of the Member States to achieve aims determined in Art. 3 of the Treaty;
- Art 119(2) TFEU – determining the obligation to coordinate in relation to monetary and exchange rate policy, which is to be implemented in a uniform way, i.e. as a single monetary policy and a single exchange rate policy.

The referred provisions indicate the field of the EU and the Member States coordination actions. However, on the basis of the general obligation to coordinate economic policies, special emphasis was put on monetary integration under single currency, euro. Coordination actions in this field are more intensive than in other fields, as a result of which monetary policy and exchange rate policy have uniform character for the states participating in the Eurosystem. The remaining countries are covered by the so-called derogation, i.e. they are at the second stage of economic and monetary union (except for the UK).

Having regard to the mentioned regulations, economic policy coordination is conducted in the EU in the following forms (European Commission, Directorate-General for Economic and Financial Affairs, 2002: 4):

- single policy, in which the Union has exclusive competence, what means that it acts independently. The centre creating directions and taking decisions with regard to policy implemented in this form was placed on a transnational level – in the Union structures. The role of the Member States is mainly to adopt these directions and to participate in the realisation of the policy according the established principles. In the form of a single policy are implemented: monetary policy, exchange rate, customs, competition and budgetary policy, whose main instrument is the EU general budget;
- close coordination, which is based on the division of competence between the Union and the Member States. It consists in the fact that general aims which are to be achieved are determined by the Union bodies and the Member States have the freedom to select instruments to achieve these aims. Examples of policies coordinated in this way are tax policy (by tax harmonisation), structural policy connected with the functioning of internal market, the EU single market, budgetary

policy in relation to budgetary balance and public debt of the Member States as well as in the scope of conducting budgetary surveillance in relation to them;

- weak coordination having very general and broad character, but legally non-binding for the Member States. Therefore, it is implemented with the use of "soft" instruments such as guidelines, opinions or recommendations, and the Member States exercise it on a voluntary basis, e.g. budgetary policy in relation to the quality of public finance.

2.2 The scope and internal structure of the EU financial law

Determining the structure of the EU financial law is quite complicated owing to a non-uniform character of provisions (norms) constituting this law. Not without a reason the Author started consideration on the principle of conferral and division of competence which impact the diverse character of the Union economic policy. The instruments used to implement it are provisions, some of which make the EU financial law. Thus, the specificity of the EU financial law consists in a complex character of the Union regulations. They may be classified according to various criteria, in particular: the criterion of the subject (scope) of regulation, addressees, validity and application. At the same time these criteria may be used to determine the structure of the EU financial law.

It seems that the key criterion is the subject (scope) of regulation of financial law, with which is connected also the criterion of addressees. It is justified by the division of the Union competence into exclusive and shared and by the coordination of economic policy. Additionally, not without significance is the criterion of validity and application of the EU financial law, but due to limited framework of this publication it is not discussed here. Therefore, having account of the provisions regulating EU public finance, its financial law may be discussed in the narrow (*sensu stricto*) and broad (*sensu largo*) sense.

2.3 EU financial law in the narrow sense

The EU financial law in the narrow sense will mainly consists of provisions concerning the Union finance as a separate organisation. Additionally,

they are connected with policies implemented in a single form. These provisions regard monetary system of the EU, central banking and its financial management, based on the general budget as well as on other extra budgetary institutions. Therefore, they create a kind of "EU finance law" or "law on the EU finance". Specifying the scope of the EU financial law *sensu stricto* it should be indicated that there are legal regulations regarding:

- economic and monetary union, including the functioning of the European System of Central Banks with first and foremost European Central Bank;
- multiannual financial planning whose main instruments are multiannual financial frameworks (financial perspectives);
- general budget of the EU, in particular its revenues, expenditure (including financial instruments), procedure of adopting and exercising budget, discharge procedures and budgetary control, protection of the Union financial interest;
- extra budgetary institutions and financial instruments, e.g. executive agencies, decentralised Union agencies, European Investment Bank, European Investment Fund, European Development Fund;
- customs union.

The addressees of this group of provisions will be Union bodies (institutions) as well as the Member States. For the former they constitute regulations whose subject is the Union financial system. In turn, compliance with legal and financial norms of this type by the Member States is justified by their membership of the EU, the consequence of which is the exercise of rights given to them as well as being subjected to the duties imposed on them, e.g. transferring revenues to the Union budget, spending resources from the EU budget within determined funds (so-called shared management of the budget).

2.4 The EU financial law in a broad sense

The EU financial law in a broad sense, besides regulations regarding financial system of the Union itself, also includes regulations which serve to build internal market and realisation of the principle of free movement of goods, people, services and capital. The addressees of the second group

of provisions are mainly the Member States. Their basic duties include either realisation of norms directly arising from the Union acts or implementation of the Union law and ensuring its effectiveness in national legal orders (total implementation of the EU law). Thus, these provisions will be directed only to the Member States. The role of the Union institutions will be limited to control over performing these obligation and applying legal requirements towards the states which infringe in this scope, e.g. by starting preliminary procedures by the European Commission or addressing complaints to the Court of Justice of the EU on the basis of Art. 258 TFEU.

Among norms of the EU financial law *sensu largo*, the ones which will be exclusively directed to the Member States, may be indicated provisions regarding:

- fulfilment of the convergence criteria, in particular fiscal rules (Zawadzka-Pąk, 2017: 111);
- compliance with the so-called reference values of budget deficit and public debt of the Member States;
- keeping budgetary surveillance in the Member States in various aspects, e.g. budgetary planning, transfer of programmes and reports, implementation of excessive imbalance procedure in the Member States (Zawadzka-Pąk, 2017: 111);
- tax harmonisation and administrative cooperation in tax issues;
- EU single financial market (Jurkowska-Zeidler, 2017: 381–382).

The above provisions are in majority covered by the frameworks of directives, what implies the need to their implementation by the Member States pursuant to Art. 288(3) TFEU.

3 Features identifying financial legal act

Different notions of a legal act appear in the doctrine of law. It may be defined very broadly, i.e. any behaviour by any person with authority acting within the legal system (Friedman, 1987: 25). However, for the purposes of this paper the Author assumed a bit narrower sense of the legal act which covers by its scope formalised actions of a public body (EU institution) within the competence granted to it and causing defined legal consequences.

This definition includes both acts making the law (normative acts) as well as applying the law (individual decisions, judicial decisions).

Moving to distinguish features identifying a financial legal act it needs to be stipulated that the Author does not identify it only with "legal-financial act" (individual financial act) – institution known in financial law as application of law act (a special type of administrative act) which has features of individualisation and specification.

Main features distinguishing a financial legal act in a given legal system include the following.

Firstly, the subject of regulation, which is public financial management of a public body. Conducting such management should be characterised by intentionality and awareness of formulated aims. It will consist in conducting financial (economic) policy with the use of proper instruments, e.g. normative acts, individual decisions. Therefore, in fact also financial policy will be the subject of regulation of financial legal act and it will be comprised of not only actions from managing public funds but also monetary system of the state or specific organisation, in particular the EU.

There is no doubt that the EU conducts defined financial (economic) policy, but as the Author has indicated, it has its own specificity. Therefore, its bodies establish legal acts which are instruments implementing this policy.

Secondly, intentionality of financial legal regulations. The main aim (justification) of financial legal acts established by public bodies is to regulate particular issues from financial management. In other words, such management is the basic aim for which the legal act passed or issued. It is important due to fact that most of provisions or decisions (rulings) causes bigger or smaller results in public finance, but not all will be classified to the category of financial legal acts.

Thirdly, the character of norms arising from the content of financial legal acts. These norms will be of imperative-attributive character, what is caused by the fact that financial law is a public law (Kosikowski, 2003: 57). As a consequence, legal and financial norms will regulate legal relationships, in which will be no equivalence of parties. Basically, a privileged party are public bodies which will impose certain financial obligations and expect proper

behaviour of the party obliged to act or refrain from performing certain actions (duty to pay taxes, duty not to exceed the amount of budgetary expenditure or maintaining financial discipline).

Fourthly, specificity of some norms arising from financial legal acts. These norms, besides classic regulation of certain behaviour, i.e. generally and in abstract, very often sanction economic phenomena, processes of managing financial resources, which have numeric (specific) aspect. In the legal-financial doctrine due to the subject of regulation formulated in such a way, was created a concept of specific norms whose content includes mentioned processes and which were defined as parametric norms (Gajl, 1992: 49).

Moreover, financial legal acts often regulate future and uncertain processes and their validity is limited in time, what in particular refers to financial plans. In this context appear so-called planned norms which are subjected to the processes of "expiry" due to time or due to their implementation.

4 Typology of the EU financial legal acts

4.1 Criteria of typology of the EU financial legal acts

Typology of the EU financial legal acts proposed below is based on the criterion of regulation manner of the EU financial policy (public financial management) and in a broader scope – economic policy as well as on the criterion of the character of the legal content. Such typology could also be conducted on the basis of the form of legal acts which usually determine legal character, but not always. Such situation is in the EU law, in which legal character of the Union acts is also analysed on the basis of functional criterion, but not only with regard to form which they have or procedure based on which they are adopted (Hartley, 2010: 108–109). In the case of functional criterion, the subject of analysis is the aim (significance) for which a given act was established.

Moreover, in the structure of legal acts in the EU secondary law, legal form does not prove its specified legal rank, including superior position. This results from the fact that the rule of hierarchy within secondary law is at least disputable and questioned by some representatives of the doctrine

(Lenaerts, Van Nuffel, 2011: 818). Therefore, financial legal acts distinguished in the types presented below are non-uniform regarding their legal character.

The proposal to make a typology of the Union financial acts mainly on the basis of the criterion of the manner of conducting financial management seems justified in the context of the above analysis. The Author indicated that such management as the subject of the acts' regulation constitutes the main feature identifying the group of financial legal acts.

The proposed typology of financial legal acts is of "framework" character. Due to limited number of pages of this paper, the Author indicated only the most important features with some examples. However, within particular types more precise analysis of legal acts may be done.

4.2 Regulatory acts

As a rule, provisions of regulatory acts determine the conduct of financial management in abstract and general manner. This will be acts of normative character, constituting the basis to formulate legal norms. Abstract character of these norms causes that their application will be repetitive until their formal abrogation in a proper legislative procedure. As a result, they will not "expire" after single application.

In turn, addressees of these acts determined in an abstract way cause that on the one hand their scope will be common, i.e. addressees will be the Union institutions, the Member States and units (e.g. regulations and general decisions) or only Member States (but without indicating particular states) and units under certain conditions (directives). On the other hand, regulatory act may be binding only within organisational structure subordinate to the body which issued it (act of internal character).

Therefore, regulatory financial acts are law-making acts and belong to the sphere of law-making. They are in the following legal forms determined in Art. 288 TFEU: regulations, directive and general decisions, including delegated and implemented acts. This group includes, for example:

- Council decision of 26 May 2014 on the system of own resources of the European Union (OJ L 168, 7. 6. 2014, p. 105);

- regulation (EU, Euratom) 2018/1046 of the European Parliament and of the Council of 18 July 2018 on the financial rules applicable to the general budget of the Union (…) (OJ L 193, 30. 7. 2018, p. 1).

4.3 Planning (strategic) acts

Planning acts of strategic character include planned norms whose content will be to forecast particular actions within the EU financial (economic) policy. In connection with the fact that these acts refer to the future, their provisions (norms) will not be binding.

Planning acts will belong to the sphere of financial management but of long-term character, i.e. exceeding one financial (budget) year. Both the long-term nature as well as the lack of binding nature will distinguish these acts from short-term operational (ongoing) plans (Stoner, Freeman, Gilbert, 2001: 263–265).

Planning acts are in the forms of strategies, guidelines, recommendations, etc., and among them the act of financial content is, e.g. Council recommendation (EU) 2015/1184 of 14 July 2015 on broad guidelines for the economic policies of the Member States and of the European Union (OJ L 192, 18. 7. 2015: 27).

4.4 Current financial management acts

Current financial management acts belong to the sphere of the application of law, and having regard to their subject of regulation – they will implement provisions of the Treaties and regulatory acts in the scope of conducting EU current financial policy. They will be issued on the basis of regulatory acts or directly on the basis of the Treaties. Therefore, norms resulting from current financial management acts will be of concrete character.

In turn, due to the scope and the character of addressees, these norms will have individual dimension. The addressees of the current financial management acts will be indicated by name: Union institutions, the Member States and units.

Basically, the group of current financial management acts will include:

- individual decisions, referred to in Art. 288 sentence 2 TFEU;

- budgets distinguished from the general budget of the EU institutions, e.g. decentralised executive agencies;
- rulings of the EU Court of Justice on financial matters.

4.5 Mixed acts

As the name suggests these acts include different features which possess acts from the above mentioned groups. This may be features typical for the law-making acts, application of law acts as well as at the same time there might appear planned norms. As a consequence, provisions of mixed acts show both binding and unbinding character. Due to this non-uniformity the Author classified them as a separate category.

An example of such acts may be the EU multi-annual financial frameworks adopted in the form of a regulation (currently – Council regulation No 1311/2013 of 2 December 2013 – OJ L 347, 20. 12. 2013: 884) and the Union general budget. On the one hand, both documents should be determined as financial plans of different duration. Financial frameworks are established for 7 consecutive years (currently 2014–2020), whereas budget for one year. On the other hand, they include planned norms in the form of amounts which in a specific scope are binding, e.g. expenditure ceilings. What is more, annual budget is the basis of the Union financial economy. There are more such diverse elements in the mixed acts.

5 Conclusion

Considerations made in this paper allow to positively answer the problems stated in the Introduction. Thus, also the stated hypothesis regarding the existence in the EU financial law a separate category of legal acts with defined identifying features, i.e. financial legal acts, should be verified.

First of all, it needs to the stated that despite the lack of formal distinction of the EU financial law in the European doctrine, it is possible to talk about regulations (norms) which comprise this law. EU financial law indicates its specificity and its scope is determined by firstly – principle of conferral and division of competence in particular fields between the Union and the Member States, and secondly – the character of financial (economic)

policy of the whole Union. In the implementation of this policy also the Member States participate and that is why it must be conducted in specific coordination forms.

Legal provisions regulating EU public financial activity, and thus regulating its financial policy, in fact comprise the EU financial law, which due to the mentioned coordination forms of this policy will have two scopes. Namely, financial law *sensu stricto* will be created by legal regulations regarding the finance of the Union as a separate organisation. They are connected with policies implemented in a single form. These regulations determine Union monetary system, central banking and its financial management based on its own budget. The addressees of this group of provisions are both the Union bodies (institutions) as well as the Member States. In turn, financial law *sensu largo*, besides regulations regarding the Union financial system, also covers the ones which serve to build internal market and implementation of the principle of free flow of goods, people, service and capital. Member States are the main addressees of these norms.

The above provisions within the Union secondary law established in proper forms comprise the EU financial legal acts. The Author distinguished this category due to particular characteristic features: the subject of regulation which is financial management (EU financial policy), imperative-attributive character of the norms resulting from these acts as well as the presence of parametric and planned norms, although this is not a rule.

At the same time on the basis of the criterion of the regulation manner of the EU financial policy (public financial management) and the criterion of the character of legal content, the following types of the EU financial legal acts may be distinguished: regulatory acts, strategic planning acts, current financial management acts as well as mixed acts.

Beyond the framework of this paper was the issue which financial legal acts will be the sources of the EU financial law, what should to be the subject of a separate publication.

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Value Creation as the Foundation of Digital Turnover Tax in the EU

Petr Vodák[1]

Abstract

The rapid growth of digital economy on the global level requires rethinking of the current international taxation framework as the profit allocation mechanisms build around criteria of physical presence do not reflect new possibilities of doing business on a global scale. This article aims to introduce and critically assess the interim legislative proposal of European Commission designed to allocate the taxing rights to the jurisdictions where the value was created. The author also evaluates whether value creation as itself is an apt concept for allocating taxing rights for digital companies.

Keywords: Digital Tax; Economy; International Taxation; Value Creation; EU; Corporate Tax.

JEL Classification: K34; O33.

1 Introduction

The technological advancement in the last decades has brought endless opportunities in many areas of life. The magnitude of free flow of information or the ability to collect data and make data-driven decisions are just examples of some levers that created something that is nowadays called the global digital economy. Doing business from anywhere in the world with a global reach has been transforming the way we approach and solve problems. Unfortunately, the rapid pace of so-called 'digital' creating new industries (search engines, social networks), and disrupting or transforming the established ones (media, healthcare), does not bring positives only. The new ways of doing business make it very challenging for the policymakers and regulators to follow up and sustain even competitive landscape. The area

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of taxation has been facing the same challenge. With the constantly increasing volume of international trade and frequency of global supply chains, the question where to tax profits of global businesses has been becoming more and more important and its complexity increases with the emergence of the digital economy.

The global digital economy has exposed the current fundamental tax principles and allocation mechanisms built around criteria of physical presence, that is supposed to allocate the profits reflecting in which jurisdiction was the value created. However, under the current scheme of rules, many of the global digital companies do not meet the definition of physical presence and do not allocate their profit into those countries. The ongoing debate on the international level with many points of view aims to answer the following questions:

- Should the states where the global digital companies successfully operate without physical presence have the right to tax a certain portion of their profits?
- Should global digital companies (or the digital economy as itself) have different taxation regime?
- If so, should the current profit allocation mechanism be modified beyond the criteria of physical presence or should there be other concepts introduced?

The magnitude of this problem is apparent as the outdated nature of the rules of international taxation creates also more flexible options for aggressive tax optimization and tax avoidance. At times unequal tax burden of traditional and digital companies lead to two main negative consequences: it creates an uneven competitive environment as well as negative effects on the predictability of public incomes. The need for rethinking the current tax allocation mechanisms will grow with ongoing digitalization of economy and it will not only be a matter of corporate taxation. Even nowadays there is an increased number of professions (e.g. data scientist), that can be carried out completely irrespective of the location, which leaves the physical location factor as the main allocation mechanism at question.

The currently discussed legislation on the EU level proposes two solutions aiming to create different taxation regime for global digital companies: interim

turnover tax followed by long-term significant digital presence. This work focuses on the first one and aims to evaluate approve or disprove following hypotheses:

- Value creation is an apt concept for taxing global digital economy.
- Interim solution reflects value creation as the profit allocation mechanism.
- Interim solution presents an effective way of taxing global digital economy.

2 Determining the taxing jurisdiction

Most of the rules in domestic tax law deal with two fundamental questions: what to tax and who to tax. In legal terminology, "what" represents the object of the tax and "who" subject of the tax as the two main construction elements of every tax. In international tax law, there is one more variable present: "where" to tax, representing the jurisdiction under which the tax subject has to fulfil its tax duty (Kemmeren, 2018: 72). The question of the legitimacy of taxing a subject by an entity is derived from the power of territory: one of the main definition aspects of a state. For a state to have the right to impose tax duty on a certain subject there must be some sort of nexus between the state and the subject (Gadžo, 2018: 195). The nexus in taxation refers to a certain degree of economic activity conducted on the territory of a state, setting forth two main factors: the territory and the economic activity (Gadžo, 2018: 205). The task for policymakers, therefore, is to construct the rules based on those two factors and to find the right equilibrium respecting interests of other countries, also describe the tax justification within the tax justification of other states, creating the spheres of interests in the community of nations (Gadžo, 2018: 205). The current international consensus expressed in the adoption of bilateral tax treaties on the basis of OECD Model Tax Conventions follows the idea that the profits are "taxed where economic activities take place and the value is created. To fully understand the concept of the current profit allocation rules, it is vital to understand the term of value creation more thoroughly.

2.1 Value creation

The term value creation is closely linked to the economist Michael Porter and his theory of value chain introduced in 1985 (OECD, 2018: 35). The value chain can be defined as a set of activities within an organization leading to creating a product or a service. Each step or the activity within the value chain contributes by a certain proportion of value to the final product resulting in a certain amount of profit, relevant for the tax purposes as the object of taxation (OECD, 2018: 35). The concept was developed around time following mostly business models of manufacturing companies with traditional sequential supply chains. However, in the current economic reality, the business models vary more significantly. The increased scale of globalization bringing the option of global value chains, the rapid growth of the service sector or accenting magnitude of the value of information are the main phenomenons that have forced OECD and legislators to adopt the bilateral treaties and add new rules reflecting the value creation principle more precisely.

2.2 Profit allocation mechanism in bilateral tax treaties

The need to create a coordinated system of tax rules among states to prevent double taxation arose at the beginning of the 20th century with the boom in international trade. At that time present League of Nations appointed four economists to propose a solution and create a system that would set criteria when dealing with issues of double taxation. The foundations build at that time basically prevailed until now. The current concept of permanent establishment used in bilateral tax treaties resembles the term origin of income, that was back then understood as "*the original physical appearance of the wealth, its subsequent physical adaptations, transport, its direction, and its sale*". (OECD, 2015: 25)

In the current conditions permanent establishment expresses a degree of physical and economic presence of an entity in a certain jurisdiction and creates the fundamental rule for allocation certain portion of tax rights to a particular country based on the source state principle. It was first adopted in 1963 OECD Model Tax Treaty and defined as "*a fixed place of business through which the business of an enterprise is wholly or partly carried on.*"

(Cockfield, 2003: 401) With the changes of the nature of economy and ways of doing business, several modifications of the initial system of rules have been adopted, always trying to follow the principle where the value was created. One of the adjustments to make was to broaden the definition of the fixed place and offer more factual-based criteria such as place of management. Furthermore, with enhancing possibilities how to reach customers by falling transportation costs, the definition of dependant agents concluding contracts in source countries, as well as broadening the definition to the services with the enhancement of the service sector. (Cockfield, 2003: 401) The concept of permanent establishment implies that the certain degree of the physical presence of a company in a certain jurisdiction is required to establish either taxing regime under either of these.

3 Disruption of the current international tax system by digital economy

The digital economy is not the first phenomenon that triggers the disruption of the international tax system. The whole process of globalization accelerated in the second half of the 20th century resolving into the emergence of global supply chains enabled separation and spread various parts of the supply chain and production factors across the globe into different jurisdictions at a tremendous scale. The worldwide presence of multinational companies gave them the opportunity to organize their transactions and assets in a way that minimizes their tax burden. Such an effort can be considered as legitimate when being in the boundaries of law, however, it creates significant disparities between the tax subject having and not having these options.

When talking about the digital economy, one of the biggest challenges is to define what actually falls in its scope and what to focus on when trying to modify the taxation rules. There have been many classifications published for the purposes of tax law, from more brief ones in academic journals to very detailed ones published by OECD and Commission.[2] The author

2 Both OECD policy papers (2015 and 2018), Impact assesement issued by European Commision, own framework also offer Kofler, Mayer and Schlager as well as Spinosa and Chand.

mostly identifies with slightly modified analysis provided by Spinosa and Chand including three main drivers (Spinosa, Chand, 2018: 478):

- Ability to collect data from its customers.
- Heavy dependence on intangible assets.
- The ability of customer acquisition at marginal or zero incremental costs.

All three components have the common denominator, which is the ability to conduct and organize such activities with very limited relevance of physical presence. For the purposes of the tax law it makes the current criteria build around physical presence inefficient and obsolete, all three drivers creating value in digitalized businesses are not fixed to any degree of physical presence.

To be able to provide a thorough analysis, this work focuses only on the first driver and evaluates implications of data processing for tax law.

3.1 The value of data and its implications for tax law

The digitalization enables data collection at a rapid pace and increases productivity significantly (OECD, 2018: 13). Gathering information can even be considered as a business strategy itself. Data are considered among many economists to be the main driver of the value creation and assets, many of them refer to the data as to "new oil." The ability to extract data, analyze them, transfer them into meaningful and applicable insights are one arguably the most important skills to possess in today's digital economy.

One of the main critiques of Porter's value chain is that it does not specifically reflect the value of information (OECD, 2018: 13). The sequential value chain the current taxation model connected with fixing the allocation mechanisms on physical location makes it very challenging to quantify and tax the value data collection brings, as the data are collected from the customers without any financial transaction taking place. The problem with taxing data collection lies in the fact that there is no ownership regime for the data and they are collected by the businesses from the users in the form of implicit barter transactions (Seppälä, 2017). The voices about taxing a barter transaction per se have been almost unanimously sceptical. Kemmeren points out, that the "raw" data are not very different from the raw material and makes an analogy to the raw

material of a manufacturing company that will process with a couple of sequential steps it to a product. (Kemmeren, 2018: 73). It is then the person or an algorithm that processes and analyses the data and gives it any meaning. Then, there has to be a person who applies the data or concerns it within his decision-making. Even the absence of the human factor should not be considered as a reason for the distinction as there has to be a human designing the algorithm. Taxing the raw data could, therefore, be an analogy of taxing a vertically integrated wood producer and furniture seller based on how many trees it cuts and disregarding factors such as the ability of the material intensity with which he is able to produce, value-added profits he is able to generate. The author agrees with this opinion only to the extent that it is not that simple to say the value is created where the users of the data were located. However, taking the analogy with the wood, the company has to pay for the raw material from the suppliers they want to use accordingly. For the current system to stay in place, the most convenient solution would be to create an ownership framework for data generated by the companies and to impose the tax on them as on any other transaction. The author is aware of the fact that there are far-reaching implications of such a measure and many unresolved philosophical, legal, economic and technological questions. In fact, European Commission has discussed this topic in one of its policy papers identifying some of the current problems of absence of ownership right from the standpoint of lack of growth of European Data economy as one of the pillars of European Single Digital Market (European Commission. 2017) Therefore the author suggests that the debate about ownership rights from the data perspective should be joint with the debate about taxation and the focus should be put on finding solutions convenient for both taxation regime and fostering digital economy.

4 Turnover tax as the interim solution

Many countries both inside and outside Europe have been aware of the problems related to taxing the digital economy and have adopted or are preparing their own unilateral measures. The legislative efforts have also been taking place on OECD and EU level. European Commission focused their efforts intensively to change the unsatisfactory status quo in taxing digital economy.

EC in its research argues that the traditional business models are significantly undertaxed compared to digital business models with the first one having the effective tax rate of 23,2 % on average and the second one 9,5 % on average, which leads to distortion of competitive landscape in the EU internal market. (European Commission. 2017: 19) On the grounds of this data the European Union began legislative efforts to adopt tax laws designed for digital economy and introduced two proposals: interim solution as a turnover tax and comprehensive solution as significant digital presence. According to the Commission the interim solution aims to help steering the discussions at international level that has been in a deadlock on the OECD level. The interim solution aims to implement a revenue based taxed on certain incomes related to digital economy (Council directive 2018/073). The second proposal of the European Commission aims to provide with more conventional solution that is more complementary to the current international tax system, proposing current international tax law, preserving taxation of only profits by enhancing the definition of permanent establishment with a significant digital presence (Council directive 2018/072). Those two measures present two main tools several countries have used to tackle the problems of taxation of digital economies. The work focuses on the interim solution as it is described and analysed in the following paragraphs.

4.1 Subject

Article 4 sets forth the subject as an entity whose:

- the total amount of worldwide revenue reported by the entity for the relevant financial year exceeds 750 million EUR and
- the amount of taxable revenues exceeds 50 million EUR (Council directive 2018/072, Art. 4).

The thresholds are meant to limit the scope of the directive only to large multinational companies (750 million EUR), and also only for the businesses whose significant income in the EU comes from the activities where the value is created by the users. The proposal does not work with the terminology used in bilateral tax treaties, such as place of residence or place of the effective management of the company, shifting away from the concepts currently in place.

4.2 Object

The taxable revenues are defined in Article 3 of the proposed directive. Tax subjects falling under the scope of this proposed directive would have two separate taxation regimes. There are three types of taxable revenues required to exceed 50 million threshold (Council directive 2018/072, Art. 3):

- The placing on a digital interface of advertising targeted at users of that interface (selling online advertising space).
- The making available to users of a multi-sided digital interface which allows users to find other users and to interact with them, and which may also facilitate the provision of underlying supplies of goods or services directly between users (incomes based on digital marketplace).
- The transmission of data collected about users and generated from users activities on digital interfaces (sale of data generated from user-provided information).

The proposal further specifically excludes from the scope some activities such as trading venues or crowdfunding platforms. In general, the proposal targets digital services where the value, according to the Commission, is mainly created by the user.

4.3 Allocation key and tax rate

The place of taxation is entailed in Article 5 of the proposed directive. With the user contribution being put in the center as the source of the value creation. The location of the user is the main determinant of the division of the revenues among the member states. The allocation key is set for each taxable revenue type separately (Council directive 2018/072, Art. 5):

- For the selling online advertising space: the number of times an advertisement has appeared on users device is taken into the account.
- For the making available of multi-sided digital interfaces are the two main situations differentiated:
  - in case of facilitation of underlying transactions: the number of users who conclude a transaction, irrespective of whether the users are sellers or buyers,

- in case of not involving the facilitation of underlying transactions (revenue is gained through periodic payments – subscription fees) – the number of users holding an account.

- For selling data: number of users from whom data transmitted in that tax period has been transmitted as a result of such users having used a device.

The division of the revenue and value creation is further regulated in Article 5(4) clarifying that the place from which the payment for the taxable services is made is irrespective of the taxation outcomes (Council directive 2018/072, Art. 5).

To allocate the revenue between the member states it is crucial to determine the location of the user owning an account, conducting transactions or having the advertisement appeared. All of the criteria are linked to the location of a device a user uses. Article 5(5) links that to the IP address of the device or "if more accurate, any other method of geolocation." That leaves the options open for identifying the location open to reflect better the technological advancement in this area (Council directive 2018/072, Art. /5).

The tax rate is set on unified 3 % of the taxable revenues allocated by every Member States based on the above mentioned criteria. The tax base for each Member State is calculated on the basis of taxable revenues defined in Article 3 and allocated by the allocation keys in Article 6. Articles 9 to 22 further deal with the administration and collection of tax, which are as procedural issues outside the scope of this thesis.

5 Analysis of the interim solution

The current commonly acceptable paradigm in income tax law is that the object of the income tax are only profits. The tax base is generally calculated as the difference between incomes and expenses in a certain tax period, with possible applicability of corrective measures depending on the type of tax, subject taxed or any further possible specifics defined by national legislation. The turnover tax, however, disregards this basic paradigm, leaving out expenses from the equation. When computing the tax base in the cross-border taxation (but also in-state), the amount of allocation

of the expenses is disregarded considered. Introduction and application of this concept will with no question have far-reaching consequences on the competitive strategies of the whole industries. The current widely-acceptable concept of taxing profits only is deeply embedded in every business strategy and decision making and this change will force companies to re-evaluate countless assumptions affecting almost every decision regarding the approach to market expansions, pricing strategies, growth strategies, approach to investments and innovations. (Bauer, 2018: 10). In the following chapters, there are a couple of thoughts on how the previously discussed digital business models could be affected by the proposed changes.

5.1 Threat of taxing companies at loss

Taxing turnovers can be a very dangerous game and has one important requirement. The industry the tax is about to be imposed on has to operate with relatively high-profit margins. That under the assumption that the legislators do not intend to tax companies that recorded a loss, which is not assumed as the intention of the legislators. When evaluating the possible consequences of the turnover tax, the first thing to look at are the profit margins the industry earns. According to the EU Commissioner Pierre Moscovici under whose scope the directive falls, the turnover tax could hit approximately 200 companies present in the EU (Flynn, 2018). From the most well-known ones, it is obvious that Google and Facebook are going to fall under the scope of the directive. Looking at the numbers, their average profit margins are moving around 30 %, respectively 20 %. With their revenue being generated from the online advertising almost by 100 % (39,9 from 40 billion worldwide by Facebook in the year 2017), the profit margins are going to actually clearly show what kind of tax will can be expected to be collected from them ceteris paribus, which would be equal to taxing profits amounting to 25 % at most. (YCHARTS, 2018). The fact that a company meets both thresholds amounting to 750 million worldwide and 50 m in the EU from the specific named activities means, that the minimal tax revenue due in the whole EU from one company has to equal to 1,5 million, as fulfilling the minimal threshold 50 million Euro with the 3 % tax rate and irrespective of any expenses. That, however, does not have to mean

that 100 % of the revenue of a certain company will be taxed on a revenue basis. The various business models have multiple sources of revenues and the fact that the 50 million threshold is fulfilled means that only that part will be taxed on a revenue basis. In case the thresholds will be met by companies with lower profit margins (Uber, Airbnb), the turnover tax could present a real challenge for them to be able to stay on the markets or it would have to pass the costs of the tax to either their customers or downstream users.

5.1.1 Setting limits to investments and consolidations

The profit margins could also heavily influence the strategies at which the companies will decide to pursue their efforts to capture a greater market share. The companies with the same market share and different profit margins will feel the consequences of imposing the revenue tax with a significant difference. 3 % revenue tax of a company with 20 % profit margins will not be as dramatic as at the company with profit margins of 5 %, where it would mean the corporate tax at the current computing rates of 60 %. That could definitely hurt the willingness of the companies meeting the threshold to invest as there will not be any incentive in form of deductible tax expenses. Once the threshold was met, the growth strategies would have to be rethought completely from scratch, as there generating the revenue first and optimizing costs second, when the expenses would not be a deductible tax item. The 750 million threshold can be also viewed as a red flag for the digital companies that have already met the 50 million threshold to be bought by a multinational entity that has already met the 750 million threshold. M & A market on the largest scale in the EU could be therefore significantly affected by this proposal as well.

These are some of the examples of how the turnover tax could heavily affect the competitive strategies as we know them today. It is difficult to predict whether the legislators have taken all of those factors into consideration as very few of the economic issues were addressed in the impact assessment, which was also the subject of criticism (Bauer, 2018: 3).

5.2 Double taxation

As previously mentioned, the foundation of the international tax law lies in the network of thousands of bilateral tax treaties adopted on the basis of the model tax treaties designed by OECD or UN. Every unilateral measure interfering with the cross-border tax regime and not reflected in the double tax conventions has the potential to create the issue of double taxation (Ismer, Jescheck. 2018: 46). The imposed turnover tax should be credible from the corporate taxed or already adopted separate taxes of each member state, as presumed by the Commission in its Impact Assessment (European Commission: 73). However, the directive does not reflect sufficiently its relationship to the other legal sources and remains silent in the matter of bilateral tax treaties and also possible conflicts with the current domestic tax laws. (Koefler et. al, 2017: 525) The member states with already adopted turnover taxes such as Hungary would probably be reluctant to dismiss their newly adopted legislation as those two tax regimes aiming at the same revenue do not seem to be able to function next to each other.

Even more politically sensitive is the relationship of the proposed directive to the bilateral tax treaties. The newly adopted tax regime would interfere with the allocation mechanisms there set. These issues can be further divided into the tax treaties the member states have among themselves and they have with the third countries. The turnover tax revenue can be allocated to one member state, that would be according to the double tax treaties allocated to another member state, but also to a non-EU state. There is at least a theoretical assumption that during the discussions around the adoption of this directive the member states would have the possibility and the ability to propose the solutions regarding modifying the bilateral tax treaties. However, in case of double taxation concerning third countries, there does not seem to be any way how to prevent such a situation within the EU legislative process. In general, it is virtually impossible to conceptually change any regulatory landscape based on the bilateral legal act by unilateral actions of one party. (Schippers, Verhaeren: 2018: 64). Considering the invasiveness of the measure of the revenue tax, any double taxation on the larger scale caused by the EU turnover tax has the potential to trigger an "international tax war" (Cockfield, 2018: 1331).

5.3 Ring-fencing digital economy

The author also warns before viewing the digital economy as something that would be able to function separately from the rest of the economy and therefore had different taxing rules. The presented analysis of currently most common business models suggested that one of the main differentiators of digital economy from traditional economies is the ability to collect and monetize data. However, these phenomenons are penetrating into all industries and it is only the pace of the changes that differ. Eventually, all industries will be somehow "digital," implementing specific features currently concentrated mostly in new and innovative digital business models (De Wilde, 2018: 475). With so-called "ring-fencing" the economy, creating thresholds and many other tools the lawmakers are creating room for issues hampering growth, market distortions, arbitrary taxation, and many other issues. With the ongoing digitalization, the legislators by pursuing this way are preparing themselves and all, including traditional businesses for another challenge of resetting outdated thresholds and excessive compliance costs due to the different tax regimes in terms of jurisdiction but also unclear areas of types of income. Another incoming challenge regarding data collection awaits with the incoming phenomenon of internet of things, already expanding exponentially the amount of data collected, with the potential to penetrate into all and currently non-digitalized industries. (De Wilde, 2018: 475). Additional taxation regimes in that case will not be something related solely to digital economy.

5.4 Feasibility of OECD solution

The ideal scenario would obviously present broader consensus at OECD level as the source of the current legal international tax framework. There have been many papers and analyses of the current situation in taxing digital economy by OECD, however, the specific solutions are blocked by the contradictory positions of particular states on the question of digital economy. However, OECD does not operate in a vacuum and has to reflect opinions of the member states. The last update from OECD on this matter reflected best the current status quo and differentiates member states into 2 main groups, one seeing the need to provide specific taxation regimes for

digitalized business models, and the other one not seeing significant needs to do so. The opinions on whether the whole international tax system should be fundamentally reformed also differ (OECD, 2018: 175). The EU position comes mainly from the fact that the European digital economy is very marginal compared to domination of the digital economy by U.S. tech companies (Howmuch, 2018). Due to this fact the negotiations on OECD level seem to be in the deadlock.

6 Conclusion

The economic arguments against double taxation are very relevant and its adoption could slow down the growth of digital economy in the EU. The risks of double taxation and triggering international tension on tax matters are very probable and should be taken into consideration. On the other hand, the turnover tax can be at this time considered as the action that is on the highest possible supranational level and would prevail fragmentation of regulation at least from the perspective of the EU countries that is likely to come as a significant number of countries are considering implementing similar measures. The turnover tax can be therefore accepted more as a risky political measure to foster action on OECD level rather than an effective sustainable measure. The author, however, is not confident about the interim nature of the measure as the adoption processes in tax matters on EU level requiring unanimous measures could present significant complications with the next changes.

From the three initial hypotheses the author reached following conclusions.

Value creation is not an apt concept for taxing digital economy as the non-physical nature of the digital economy makes it very difficult to assign various parts of the value chain to specific jurisdictions giving too much room for the digital companies to create "paper profits." Furthermore, due to of lack of ownership in data economy and data collection in form of quasi-barter transactions there are very limited options to quantify the value added.

Interim solution in the form of turnover tax does not reflect value creation as the profit allocation mechanism as it fixes the allocation rule only on the first step of the value chain creating the fiction of value creation.

Interim solution presents an effective way of taxing global digital economy in terms of volume of tax revenue and as a tool to create pressure to pursue more fundamental changes, however, with the following very significant disadvantages, such as threat of taxing companies at loss, slowing down growth of digital economy and limit incentives to invest, as well as inevitable double or multiple taxation.

The foundations of the current international tax system date back to the beginning of the 20th century, when it was literally unthinkable that one product could be the result of a global supply chain taking place in several countries, or that there would be a possibility to dominate foreign markets without any physical presence. In the current conditions, value creation is not a suitable approach for taxation of the digital economy as the main drivers of the digital economy are either difficult to quantify (intangible assets) or lack ownership framework and are gained mostly by barter transactions (data). Fixing value creation on user location seems rather artificial as data themselves do not create any value, it is people or algorithms designed by people, who process them and give them meaning, as well as the executives making decisions based on them. If the tax justification were to be led purely by the value creation principle, the data themselves would not account for 100 % of the value creation, the same way raw input does not create 100 % of the value of the product. The difference between wood and data in this example, however, lies in the fact that in case of wood there is an identifiable economic transaction that can be subject of tax, whereas in case of data, there is no such transaction between the users and the company.

The author does not identify with the reasoning of the Commission that the data itself can be considered as main source of value creation. As previously mentioned the data are only the input and could also be considered as the upstream stage of virtual value chain, not the final product or service. Commission rightfully points out that the value chain starts at the data collection from customers, where the data are collected and further used.

However, there is no revenue generated to the customers and therefore no financial benefits to either them or the states. The economic benefit lies in using the service, usually referred to as a factual barter transaction, where no financial performance is conducted, therefore there is nothing to tax. This phenomenon is referred to as "lack of ownership rights in data."

This legal vacuum should be somehow addressed and the value transferred from consumers to companies should be reflected somewhat more corresponding than quasi-barter transactions. The fiction of assigning value creation is not a sustainable solution and does not reflect the concept of value creation but rather creates a fiction of value creation. It is fair to point out that the switch to the immobile factors not bundled with value creation (i.e. user location) is something that would limit the tax planning opportunities of global companies. Such a significant change would mean restructuring system of corporate taxation from scratch.

However, given the deadlock of the OECD reforms and possibility of finding any progressive solution on the multilateral level is nowhere near, this proposal can be understood as a legitimate way how to create political pressure on fostering change in the whole international tax system. Commission has to be aware of the fact that such invasive actions have the potential to trigger retributive measures especially from the US side. The situation looks quite similar to the current situation in the field of international trade. In that case, US Administration has been accusing other countries of not following rules in the field of intellectual property, especially China, and imposed tariffs on certain goods. Here, the EU is the one losing tax revenue mostly because of dominance of US tech companies on the European market and their avoidance of tax rules, therefore it aims to create pressure on other countries by introducing invasive measures.

The interim solution presents a unilateral change resolving into double or multiple taxation conflicting with allocation rules adopted on national level and rules contained in bilateral tax treaties. The ideal solution would present consensus on OECD level either as either modification of bilateral tax treaties, or ideally creating global platform similar to WTO. The lack of political consensus due to different interests of countries, mainly United States and EU, prevents from reaching consensus on OECD level. In that

case, the turnover tax proposal can be understood more as a mean of creating political pressure rather than a sustainable solution. The turnover tax proposal could significantly hamper growth of digital economy in the EU and could also trigger retributive measures from non-EU countries. Therefore, before determining what should be done, it is important to firstly determine who should be doing it. The most important feature of any implemented solution is not how it looks like but how universal it is. The ability to reach global changes is currently limited by the bilateral nature of sources of international tax law in bilateral tax treaties. The platform, where the consensus should be reached is OECD, however, none of its documents are binding for any of the countries. The same way the international community reacted with the emergence of international trade caused by first unbundling by creating WTO, the ideal way would be to create the same multilateral platform that should react on the second unbundling and emergence of global supply chains as well as digitalization in field of taxes and focus common efforts to redraw the current profit allocation rules from scratch.

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Implementation of the Exit Tax to the Polish Legal System

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Abstract

This contribution deals with an obligation of the exit tax implementation to the Polish system of tax law the directive 2016/1164 related to the rules against tax avoidance. It is necessary to examine the variable elements of the legal structure of the exit tax.

The main purpose of the paper is to confirm or disprove the hypothesis that implementation has been carried out correctly and concerning European freedoms. The primary scientific method is the analysis of European and Polish sources of law. The latest case-law and selected doctrinal works will be used in the contribution. Empirical research, both in terms of hypothesis and effects, is to help in a better understanding of the phenomenon and formulation of *de lege ferenda* postulates.

Keywords: Exit Tax; Tax Avoidance; Taxation; Emigration.

JEL Classification: H24; H26; K34.

1 Introduction

The issue of the income tax is connected inextricably with the problems of globalisation and economic freedom. Cross-border capital transfer or change of tax residence is of the interest to many tax legislators, including the EU ones. It is dictated by notable amounts, which may constitute a significant budget supply for the leaving and entering countries.

The concept of exit tax and the scope of indispensable implementation resulting from the European Union regulations have to be considered.

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The study will be conducted based on the wording of the Personal Income Tax Act of 26 July 1991, as amended (hereinafter: PITA) as well as the Corporate Income Tax Act of 15 February 1992, as amended (hereinafter: CITA). By analysing the applicable legal acts, it will be possible to answer the question about the correct implementation of the legal institution unknown in Poland which is exit tax. The purpose of this article is to analyse and evaluate the applicable provisions aimed at taxing the cross-border transfer of certain assets or changing tax residence. The thesis will be subject to the examination as to the correct implementation of the Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (hereinafter: Directive ATAD). Next important regulation is the Council Directive (EU) 2018/822 of 25 May 2018 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements. The latest case-law and selected doctrinal works will be used in this paper. Empirical research, both in terms of hypothesis and effects, is to help in a better understanding of the phenomenon and formulation of *de lege ferenda* postulates.

As mentioned above, the exit tax institution is not widely known by Polish tax law. Many authors examined tax competition aspects. So far, these issues have been addressed by Armstrong, Blouin, Jagolinzer, Lacker (Armstrong, Blouin, Jagolinzer, Lacker, 2015), Atwood, Drake, Myers J. N., Myers L. A. (Atwood, Drake, Myers J. N., Myers L. A., 2012), Cerioni (Cerioni, 2013), Bucovetsky (Bucovetsky, 1991), Chyz (Chyz, 2013), Devereux, Loretz (Devereux, Loretz, 2012), Dzialo (Dzialo, 2015), Fouquet (Fouquet, 2002), Kubicová (Kubicová, 2016), Kovács (Kovács, 2009), Langenmayer (Langenmayer, 2015), Marianski (Marianski, 2019), Nowak-Piechota (Nowak-Piechota, 2019) and Panayi (Panayi, 2011).

The term exit tax is known by EU regulations and some countries, both EU and non-EU. In addition to the amendment of the provisions on the general clause against tax avoidance (GAAR) and the introduction of the obligation to submit tax information to tax authorities, it is part of the broader plan of the Ministry of Finance aimed at tightening the income tax collection system. These regulations have been in force in Poland since

the beginning of 2019. The individual elements of the legal construction of exit tax require consideration. They allow to qualify it to the income tax group.

2 The scope of the exit tax concept

The exit tax institution has been operating in the Polish tax law system since 1 January 2019. The Act of 23 October 2018 introduced it on the amendment of the Personal Income Tax Act, the Corporate Income Tax Act and the Tax Ordinance Act and other legal acts (hereinafter: the amending Act). The exit tax is also called a tax on unrealised profits or tax on moving out (emigration).

It is worth noting that there was an attempt to introduce into the internal legal order in 2013 as a kind of exit tax in Poland. Then the draft law was assessed as violating the EU principles of the freedom of entrepreneurship, the flow of capital and the constitutional principle of discrimination, and finally, the work on it was discontinued.

As it has been established, the introduction of the exit tax is connected with the necessity to implement the ATAD directive by Poland, aimed at counteracting practices related to the tax avoidance. In principle, the provisions of the directive cannot be applied directly. The practices in question directly affect the intra-EU market. This leads to a reduction of domestic tax revenues, which makes it difficult for the member states to conduct pro-growth tax policies.

The definition of the tax avoidance has a doctrinal and normative dimension. By Polish law, tax avoidance means all legal activities of the taxpayer, aimed at reducing or eliminating the tax burden. The opposite of tax avoidance is the concept of tax evasion, which presupposes a direct violation of tax law regulations, often as a result of activities in fraudem legis (Juchniewicz, 2017: VII).

The current political priorities of the international taxation (mainly OECD and EU) emphasise the need to pay taxes at the place of generating the profits and value. According to art. 5 of the ATAD Directive, taxation of unrealised capital gains occurs when assets, tax residences or a permanent

establishment are transferred. In other words, the obligation to pay an exit tax results in a change of the tax residence, as well as an international transfer of property or even a part of it.

The essence of tax exit taxation is the adoption of a legal fiction from which the taxpayer is considered to sell certain assets and therefore has to pay a special tax. It is about the possibility for the Member States to counteract the practices of some taxpayers, seeking to reduce the level of taxes paid by transferring their tax residency or assets to a less-oppressive jurisdiction. As a result, the internal market is disturbed by the erosion of the tax base of the state of departure and shifting future profits to a country with lower taxation. As a result, the state from which the taxpayer transfers his residence or assets is deprived of the future right to tax his income (income), which, by the way, has not yet been realised, although it could have already been generated. It should be emphasised that the tax description does not change the owner of the assets.

The moment the tax obligation arises in the context of the transfer of property abroad, under art. 30da/6 of the PITA, is the day when the asset is transferred outside the territory of the Republic of Poland preceding the day on which the asset ceases to be allocated to activities carried out on the territory of Poland, including through a foreign establishment. This provision leaves no serious interpretation of doubts. However, it is problematic to determine the date of the tax obligation when it comes to the transfer of a tax residence. In this case, the Act does not define how to determine the moment the tax obligation arises.

3 An entity subject to the exit tax

The entities obliged to pay the exit tax are the taxpayers of personal income tax and corporation tax. Cases with which the Amending Act relates to the payment of the tax concern the transfer of a legal or natural person's asset beyond the Polish tax jurisdiction, change of tax residence by a taxpayer subject to unlimited tax liability – if Poland loses in whole or in part the right to tax income from the sale of a specific component property in the context of its transfer abroad or change of the place of residence of the taxpayer,

or its registered office or management to another country. It should be emphasised that the tax on unrealised profits is subject to such a cross-border transfer of the asset component, as a result of which this component remains the property of that entity. The legislator did not explain the meaning of the term "transfer of assets outside the country". He only showed an example of a catalogue of situations in which this transfer takes place. It will be mentioned below. However, he introduced a condition whereby a natural person changing residence should be subject to exit tax; he must reside in Poland for at least five years in ten years before the change of tax residence.

The ATAD Directive makes the obligatory implementation only for the corporate income taxpayers. The Polish tax legislator also taxed natural persons conducting business activity. However, he did not stop there, but went much further and included to the taxpayers exit tax, under certain conditions, the natural persons not conducting business. It exceeded the instructions set out in the ATAD directive. Article 1/1 of the directive indicates that the directive applies to all taxpayers who are subject to corporation tax in at least one Member State, including permanent establishments resident in one or more member tax in a third country. These rules should apply to all entities that are treated by the state as clear (transparent) for tax purposes. Tribute imposed on natural persons, especially those not conducting business activities, constitutes a violation of the provisions of the ATAD Directive. It is specifically about art. 1 in connection with art. 3 and art. 5 of this. This directive is the minimum level of protection recommended to the Member States as a remedy for the phenomenon of aggressive tax planning. Also, the amending Act violates art. 49 of the Treaty on the Functioning of the European Union: no. 2012/C 326/01 (hereinafter: TFEU), which will be the subject of the analysis of the next part of the study.

4 Subject matter and tax base exit tax

The particular nature of the exit tax is highlighted in the construction of the subject of taxation. The essence of the exit tax is the adoption of a legal fiction associated with the assumption of the disposal of property or change of tax residence to a foreign jurisdiction. The tax subject to exit tax is the hypothetical

income (revenue) that a taxpayer would have to achieve. The subject of the taxation is not the actual income (revenue) but determined by the theoretical presumption of achieving not-gained profits from the sale of certain assets. In this way, states defend themselves against the erosion of the tax base in the Member States, estimated at EUR 50–70 billion per year (COM (2016) 26 final–2016/0011 (CNS)) and the so-called phenomenon of the artificial emigration. The exit tax is for them a tool to fight tax avoidance. A favorite tool, among others, in France, Germany, Spain, Norway, the USA and other countries (Kubicová, 2016: 1107). EU member states, according to ATAD, decided to tax the market values of assets transferred to other countries in four cases:

- transfer of assets from the registered office to a permanent establishment,
- transfer of assets from a permanent establishment to a registered office or another permanent establishment,
- change of tax residence,
- transfer of a permanent establishment.

Taxation of unrealised capital gains may be subject to postponement for a minimum period of 5 years, provided that transfers are made within the European Economic Area countries. In the literature on the subject, it was noted that the solutions developed over the years effectively protect entrepreneurs from double taxation, but do not protect the countries sufficiently against tax evasion. Considering the abuse of regulations regarding transfer prices, as well as (raised in the OECD reports under the BEPS initiative) the problem of overly developed tax advisory departments related to aggressive tax planning, it is not surprising that the regulations should be tightened (Gluminska-Pawlic, 2018: 3).

The Polish legislator, when implementing the ATAD directive, established an open catalogue of events giving the rise to the tax obligation. It has a broader scope than the one resulting from this directive. Based on article 30da/4 of the PITA and art. 24f/3 of the CITA, a catalogue of cases that are examples of the transfer of an asset outside of Poland, concerns:

- transferring by the taxpayer, to his plant outside Poland, the property component so far related to the activity carried out in Poland,

- transferring, to your country your tax residence or another country in which the company operates through a foreign plant, an asset previously associated with the activity carried out on the territory of Poland by a foreign plant,
- transferring, by the taxpayer to another country, all or a part of the activity carried out so far by the foreign plant located in Poland.

Besides, according to art. 30dh/3 of the PITA and art. 24k/3 of the CITA, free transfer of an asset to a third party located in Poland, as well as contributing an asset to an entity other than a company or cooperative is also subject to the taxation, if in connection with this transfer or contribution Poland loses in whole or in part the right to tax income from disposal of this asset.

Although art. 3 of the ATAD Directive entitles the Member States to create more restrictive regulations; it concerns solutions of an objective (technical) and not a pro-fiscal nature. In this respect, by widening the catalogue of cases of possible taxation, the implementation was made incorrectly (Nowak-Piechota, 2019: 34–40).

It is puzzling that the Polish legislator decided on such a solution in the context of public decisions of the EU Court of Justice (hereinafter: CJEU). In 2006, the CJEU considered that taxation of the taxpayers based on unrealised profits and those transferring their residence abroad – according to unrealised gains – is an example of unequal treatment affecting freedom of movement (CJEU: C-470/04). CJEU stressed that the freedom of movement of persons and the freedom of establishment are the foundations of the European legal system. Speech, among others on the De Lasteyrie du Saillant judgment of 11 March 2004 (CJEU: C-9/02), and above all about the N v. Inspecteur dated 7 September 2006 (CJEU: C-470/04). Nevertheless, in 2011 the change of the CJEU ruling line should be noted. The Court in a controversial ruling of 29 November 2011 in the case of National Grid Indus BV v. Inspector van de Belastingdienst Rijnmond / kantoor Rotterdam (CJEU: C-371/10) stated that a member state should have the right to tax profits arising in the area of his competence before transferring capital to another country. From that point on, the EU has taken some measures to tighten up the national tax systems. In this judgment,

the Tribunal considered admitting the exit tax of natural persons admissible but referred to the next collection of the tax as a violation of the principle of free movement of persons. He also commented negatively on the deferral of the tax subject to the provision of security in the form of a bank guarantee.

The adoption of defective tax regulations in the amending Act, despite also reporting critical remarks by the National Council of Tax Advisors at the consultation stage, indicates the urgent need to obtain the additional funds for the state budget. The negative mark was also imprinted on the shape of current regulations due to the crazy, only two-month pace of work. Poland has adopted exit tax regulations a year faster than the ATAD directive provides. As a result, a few weeks after the entry into force of the discussed regulations, the Ministry of Finance started work on the preparation of official "tax explanations".

The applicable provisions of the amending Act do not differentiate the situation of the taxpayer. The tax legislator assesses the change of the tax residence dictated by family, health or new place of employment in the same way as a temporary change related to the sale of assets, aimed at avoiding taxation. The legislator has recognised every natural person as a de facto artificial emigrant. The reason for changing tax residence is irrelevant. If the change of residence lasts longer than a year, in each case, it will involve the necessity to pay income tax, which the taxpayer has not obtained. This penalization of the change in tax residence for individuals is too far-reaching. The state should only tax such events, as a result of which it will irretrievably lose the possibility of taxing the capital earned in its area. By allowing taxation of natural persons on the indicated conditions, the Amending Act incorrectly implements the ATAD Directive. Violating the objectives of the Directive, it also undermines the basic principles of the functioning of the European Union, i.e. the freedom of movement of persons and capital and entrepreneurship. The amending act adopted by the tax legislator violates art. 49 TFEU in part related to the difficulties that refer to the settlement of a Polish citizen in another member state (vide: CJEU: C-251/98) and starting a business activity within the territory of another EU country (see: CJEU: C-269/09 and C-371/10).

One of the last judgement on 26 February 2019 of the CJEU – request for a preliminary ruling under art. 267 TFEU in the proceedings M. Wächtler v. Finanzamt Konstanz the Court said that the provisions of the *Agreement* on the Free Movement of Persons between the Swiss Confederation and EU must be interpreted as precluding a tax regime of a member state which in a situation where a natural person who is a national of a member state and who conducts an economic activity in the territory of Switzerland transfers his domicile from the member state whose tax regime is at issue to the Swiss Confederation, provides for the collection at the time of that change of the tax payable on unrealised capital gains with respect to shares owned by that national, whereas, if domicile is retained in that member state, the collection of the tax happens only at the time when the capital gains are realised, that is on a disposal of the shares concerned (CJEU: C-581/17).

The amended provisions in the income law in question partially constitute a violation of the principles of the Business Constitution (Act No. 646/2018 Coll., on Entrepreneurs' Law, as amended, Article 67/1). It indicates that the legislator should not introduce regulation over what is necessary for the correct implementation of EU law, nor impose further obligations on entrepreneurs or solutions that are more stringent than the implemented law requires.

Indications require different consequences of such a broad implementation. It is primarily about the possible competitiveness of the Polish economy and the reluctance of foreign investors to operate in Poland due to unclear regulations regarding exit tax. A severe problem is the limitation of the development opportunities of enterprises planning to expand abroad. Each company transferring assets to conquer international markets begins with a specific penalty for the desire to develop in the form of an obligation to pay an exit tax.

Given the above, it is necessary to postulate de lege ferenda the departure from taxation of exit tax of natural persons. The most significant doubts arise from the taxation of natural persons not conducting business activity. The severe punishment that they will have to incur when selling assets or changing their residence is a violation of EU treaty freedoms. It is about the freedom of movement and entrepreneurship, as well as the flow of capital.

Under the ATAD Directive, the national regulations should prevent the creation of new market obstacles such as double taxation. One should point out some collisions and examples of double taxation, possible after the amending Act enters into force. It is impossible to present them here, due to the volume framework of this article. Signalling: a taxpayer-shareholder who changes his residence will pay an exit tax, and then, by disposing of shares, he will pay another tax on his new place of residence.

5 The rates, terms and conditions of paying the exit tax

In a situation in which the tax value of an asset is determined, by art. 30da/1 of the PITA, tax on income from unrealised profits is 19 % of the tax base. However, if the tax value of an asset is not determined, it is 3 %. In case of legal persons, under art. 24f/1 of the CITA, one rate is valid – 19 % rate. The tax legislator, as the reason for the tax exemption of physical persons, indicates the principle of equality referred to in the Constitution of the Republic of Poland. For this reason, he determined different rates for natural and legal persons. Such explanation should be assessed as bizarre.

It should be stressed that the tax law has a new concept of "tax value", which is the cost base for the calculation of the taxpayer's income. According to art. 30da/8/2 of the PITA, the market value of the asset is determined (except for the personal assets and components, the transfer of which does not involve a change in economically significant functions, assets or risks) under the terms of art. 23o of the PITA. It is about regulation in the field of transfer prices. However, the PITA regulations do not specify how the market price principle should be used to determine and document transfer prices in the circumstances justifying the tax obligation in exit tax.

As mentioned many times, the obligation to implement exit tax results from the ATAD directive. At the same time, the deadline for implementation of the regulations is 1 January 2020. Despite shortening the period of entering into force of the tax in question relative to the ATAD directive, the legislator did not decide on longer *vacatio legis*. Less than seven weeks to familiarise taxpayers with an entirely new regulation, burdened with severe financial consequences, is not enough.

Critics should be subject to the date of payment of the tax. According to art. 30da/14 of the PITA and art. 24f/12 of the CITA, the taxpayer is required to submit a tax return and pay the tax by the seventh day of the month following the month in which the income was generated according to the valuation of the assets. As a result, the subject of taxation is a hypothetical profit. A curious situation will be the necessity to pay the exit tax even if, finally, the assets show a loss. Investments on the stock exchange may be such an example. The regulation ordering the taxpayer to pay tax immediately is a violation of Art. 49 of the TFEU in so far as it concerns the change of the taxpayer's place of residence. Such judgments are confirmed by numerous judgments of the CJEU (for example CJEU: C-470/04). The ATAD directive indicates that taxpayers should have the right to pay a certain amount of tax on unrealised capital gains or defer payment of a tax by paying in instalments over several years, or by charging interest and providing a guarantee. According to current CJEU jurisprudence, it is acceptable for the Member States to impose unrealised profits when changing headquarters or moving out. However, only immediate taxation is not allowed. In the Court's fair assessment, it is disproportionate and violates various freedoms. Providing taxpayers with alternative methods of regulating exit tax will be a sufficient *de lege ferenda* procedure, allowing recognition of the implemented provisions in this part to be consistent with applicable European law (see the CJEU ruling of 13 November 2017, C-646/153). It is about deferring taxation with the option of charging interest or the requirement to provide adequate security. It is always possible to postpone the payment of the tax until profit is realized and the amount of the tax is spread over instalments over five years. In many countries, there is no taxation of hypothetical profits, and the tax base is real capital gains. In France, if there has been no sale of assets before the lapse of fifteen years – tax does not occur, in Spain – after ten years, and in Holland, the indefinite postponement applies – the tax is charged only at the time of profit.

The necessity to pay tax on unrealised income from the disposal of assets means that the taxpayer is forced to allocate funds from other sources for this purpose. In this way, the Polish exit tax can be compared to the customs institution (toll), since the moment of actual disposal of the property

is legally immaterial. Typically, a taxpayer pays tax on real taxable activity. The construction of a hypothetical tax base implies significant oppressiveness and ambiguity of the solution. The biggest doubt is due to the obligation to pay the tax immediately. Given the above, it is necessary to postulate *de lege ferenda* postponing the obligation to pay an exit tax until the actual transaction of disposal of a given asset is completed. This proposal will partially liberalise the effect of harmful super-regulation in part concerning natural persons.

6 Tax preferences in exit tax

The Act Amending Art. 30dc/1, under the ATAD directive, assumes exemption from taxation of assets transferred outside Poland for a definite period, not longer than 12 months. The exclusion in question is subject to the condition that the transfer of this asset is directly related to the liquidity management policy of the enterprise belonging to the taxpayer, which is located on the territory of Poland and another country. The transfer of securities or other components of the property is carried out by an agreement of transfer of title to secure the claim.

The provisions of art. 30da of the PITA shall not apply if the total market value of the transferred assets does not exceed PLN 4 million. In the case of spouses, this limit applies to two of them. In CITA, the limit of the market value of assets transferred outside the territory of the Republic of Poland was not determined by the legislator. The CITA Act (Article 24g/1) includes the exclusion of credit institutions and investment firms, provided that they transfer their assets outside Poland for a period not longer than 12 months, and this transfer is carried out in order to meet the prudential capital requirements defined in the EU law. This means that exit tax will be paid by every entrepreneur who will transfer any assets needed for his day-to-day operations to his branch outside Poland if these assets are used in a foreign branch over 12 months. For this reason, it seems justified to state the anti-development character of this tax. Although it should be mentioned for the sake of order, the Amending Act provides for specific solutions in the event of a return of the taxpayer's assets to Poland.

Exemption from exit tax, based on art. 30 dd / 1 of the PITA are assets that are intended for use by employees that are directly related to the work performed, which are not fixed or current assets within the meaning of the accounting regulations. Exemption from the tax on unrealised profits also covers assets that are transferred for public benefit purposes to organisations conducting activities in the sphere of public tasks. In order to be able to apply for the exemption, the person transferring property cannot hold the right to participate in the profits or assets of the foundation or association concerned.

It should be added that there is no basis for applying the tax due to unrealised profits if Poland still retains the right to tax specific assets after the change of residence. For this reason, taxation does not refer to assets that after the change of tax residence are still related to the foreign taxpayer located on the territory of Poland, who changed the tax residence (Nowak-Piechota, 2019: 34–40). Also, due to the so-called with a real estate clause in double taxation conventions, the right to tax real estate is vested in the state where the property is located.

Besides, the possibility of spreading the payment of tax on income from unrealised profits for a maximum of 5 years is subject to many conditions (Article 30de of the PITA and 24i of the CITA). This increases the oppressiveness of the discussed solution.

7 Conclusions

This study aimed to analyse the new tax system in the Polish tax system. It has been proved that the Polish legislator has incorrectly implemented the ATAD directive. The planned publication by the Ministry of Finance of explanations to the amending Act will not solve the numerous imperfections of the new law. An urgent intervention by the legislator is necessary in various areas.

While the need to limit the erosion of the tax base in the internal market and the transfer of profits beyond European jurisdiction should be positively assessed, the fact that introducing the Polish legislator's implementation of the overregulation raises serious doubts. Penalization of change in tax residence

in case of natural persons is too far-reaching. As established, the state should only tax such events, as a result of which it will irretrievably lose the possibility of taxing the capital earned in its area. The issue of taxing the unrealised profits is connected with the problem of restricting the freedoms of the treaty. It is possible to limit them provided that the proportionality requirements are met. By allowing taxation of natural persons under the indicated conditions, the Amending Act incorrectly implements the ATAD Directive. Violating the objectives of the directive, it also undermines the basic principles of the functioning of the European Union, i.e. the freedom of movement of persons and capital as well as entrepreneurship. It also violates art. 49 TFEU in the part related to the difficulties related to the settlement of a Polish citizen in another member state and starting a business activity within the territory of another EU country. Numerous CJEU rulings confirm this position.

The most significant doubts arise from the taxation of natural persons not conducting business activity. Because of the above, it is necessary to postulate *de lege ferenda* the departure from taxation of exit tax of natural persons.

The ATAD directive indicates that taxpayers should have the right to pay a certain amount of tax on unrealised capital gains or defer payment of a tax by paying in instalments over several years, or by charging interest and providing a guarantee. According to the new case law of the CJEU, it is acceptable for the Member States to tax unrealised profits when they change their headquarters or move out. However, only immediate taxation is not allowed. In the Court's fair assessment, it is disproportionate and violates various freedoms. Providing taxpayers with alternative methods of regulating exit tax is another demand of *de lege ferenda*. This proposal will partially liberalize the effect of harmful super-regulation in the part concerning natural persons.

For all these reasons, the anti-development approach towards exit tax seems justified. This tax in its current form is a quasi-penalization of emigration.

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PART 5:
FINANCIAL LAW OF LOCAL GOVERNMENT

Participatory Budget in Poland and in France – the Direction of Changes

Monika Augustyniak[1]

Abstract:

The participatory budget consists in the right of a self-governing community to put forward motions to self-government authorities for tasks to be financed. Such undertakings should fit into the catalogue of optional tasks performed by the territorial self-government units. This legal mechanism aims at allowing residents to carry out certain public tasks they consider important, to co-decide on the allocation of financial means to projects they regard as needed. This paper aims mainly at examining how the participatory budget is organized and operated in Poland and in France in order to determine potential directions of change with regard to the operating principle of this financial instrument to strengthen active citizenship in co-managing local public space. For the purpose of this paper, a legal theory method (consisting in an analysis of a legal text) and legal comparative method were applied. The problem discussed herein has not yet been addressed by legal comparative studies, which makes this paper an innovative one.

Keywords: Participatory Budget; Self-Governance; Immediate Democracy (*démocratie de proximité*); Distribution of Power between the Representative and Direct Democracy; Two Types of Participatory Budget (community-wide and district-wide).

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1 Introduction

Participatory budget is a new instrument allowing society to participate in managing units of territorial self-government in Poland and in France. The mechanism constitutes an expression of the principle of subsidiarity and openness in execution of public authority in a democratic state.

The participatory budget[2] consists in the right of a self-governing community to put forward motions to self-government authorities for tasks to be financed. Such undertakings should fit into the catalogue of optional tasks performed by the territorial self-government units. This legal mechanism aims at allowing residents to carry out certain public tasks they consider important, to co-decide on the allocation of financial means to projects they regard as needed[3]. This paper aims mainly at examining how the participatory budget is organized and operated in Poland and in France in order to determine potential directions of change with regard to the operating principle of this financial instrument to strengthen active citizenship in co-managing local public space. For the purpose of this paper, a legal theory method (consisting in an analysis of a legal text) and legal comparative method were applied. The problem discussed herein has not yet been addressed by legal comparative studies, which makes this paper an innovative one.

2 "*In English, the expression of 'participatory budgeting' has been used from the late 1990s in order to stressthis notion of an ongoing process ('budgeting') rather than an outcome ('budget')*" [Sintomer, Y., C. Herzberg, A. Röcke, Allegretti G, 2008: 3].

3 In France, the mechanism of participatory budget is closely linked to town district councils and activities regarding participation of resident at this municipal level. Town district councils are an instrument, which enables co-management, but modest financial means enmarked for this purpose pose real problems. In 2003, the first such advanced experience within the scope of participatory budget was launching this instrument in La Roche-sur – Yon (53 000 residents), where on average, 26 000 € was allocated to a single town district (365 000 € in total) under participatory budget, which equalled to 1,5 % of the municipal investment budget. In most cases, the amounts allocated to participatory budget in French municipalities are far lower (Sintomer, Herzberg, Röcke, 2008: 125).

2 Legal basis and types of participatory budget

2.1 The notion of participatory budget and the normative context

Within the Polish legal order, the legislator has introduced the institution of participatory budget on 1 January 2019 based on systemic acts of self-government. Until that date, such budgets existed based on consultative resolutions[4]. Whether a participatory budget was launched or not depended on the willingness of a unit of territorial self-government rather than on the actual will of residents. As it stands, in all systemic acts on self-government, participatory budget is defined as a form of social consultation[5], within the scope of which residents annually decide on a portion of a given unit's expenditures through direct vote. Tasks selected for execution under the participatory budget are included in the budget resolution of the given unit of territorial self-government. While proceeding a draft budget resolution, municipality/district/provincial council can in no way remove nor change significantly the tasks selected within the participatory budget. Certain doubts arise due to the use of the discretionary phrase "significantly". However, ensuring that tasks to be financed from the participatory budget will be included in the budget and will not be modified to a significant extent via budget amendment tabled by councillors certainly guarantees that these tasks will be executed properly. The issue of participatory budget development is a rather new phenomenon and despite already existing experience, it is still relatively poorly known. What should be underlined at this point as a problem is fundamental differentiation of ways

4 Consultative resolutions within participatory budget aimed at becoming aware of the residents opinions on the proposed tasks, which could be financed from the budget of a given self-government unit. Consultations are a form of seeking resident's opinions and their results are not binding, unlike referendum, although authorities should take such opinions into account if this is to act as a form of local democracy (Leoński, 1998: 71).

5 Although consultations do not have a binding character, they should be taken into account as an expression of will of the primary public authority (sovereign), who constitutes a link to "co-participation" in exercising public authority within a self-governing community.

of consulting, failure in establishing homogenous standards for application and selection of projects (Bednarska-Olejniczak, Oleniczak: 2017).

Early French experiences on the participatory budget date back to 2000, but the instrument has been revived with the beginning of a new term of territorial community councils, that is, since 2014. French legal order lacks legal basis for establishing participatory budget. No CGCT (Code général des collectivités territoriales – general code of territorial communities) regulation provides basis to launch such a budget, nor within communes nor town district councils. However, such a practice shows that participatory budget is launched pursuant to internal regulations of communal councils (or town district councils – arrondissements – respectively) or based on charters of town district councils (*la charte des conseils des quartiers*), which counterpart the statutes of municipality's auxiliary units within the Polish legal order. For example, town district councils (*arrondissement*) in Paris passed the Participatory Budget Charter, which assumes that individual town districts shall join in the mechanism voluntarily and their resident shall participate in creating their own motions for tasks to be executed within their district of residence.

2.2 Types and material scope of participatory budgets

Within the Polish legal order, participatory budget in municipalities, districts, and provinces enables residents to participate in the decision process on allocating financial means for execution of tasks within a local community, both at a basic level (that is units of territorial self-government) and a lower level (that is auxiliary units of municipality). This means that the institution of participatory budget may function both within the basic and auxiliary territorial division of the state. In the case of districts, the legislator permits the financial resources spent within the scope of participatory budget to be divided into pools covering the entire district and its parts, that is, individual municipalities or groups thereof. On the other hand, resources spend within the provincial participatory budget may be divided into pools covering the entire province or its parts, that is individual districts or groups of districts.

From 1 January 2019, two types of participatory budget may be distinguished within the Polish legal order: obligatory and optional. Pursuant to art. 5a item 5 of the act dated 8 March 1990 on commune self-government, establishing participatory budget is obligatory in municipalities which are cities with district rights and the size of the participatory budget equals no less than 0,5 % of the municipality's expenditures included in the last report on budget implementation. In other cases, participatory budget is optional and depends on the degree of interest in such a financial form of active citizenship expressed by residents of a given self-governing community. Participatory budget constitutes a form of direct democracy of a conclusive nature (Augustyniak, 2019: 160).

Similarly, in the French Republic, the institution of participatory budget functions at the community and town district level (*arrondidssement* and *quartier*) and thus becomes an institution of democracy immediate to the citizen (*la démocratie de proximité)6*. A possibility to implement participatory budget in schools is a novelty. Such an initiative was put forward by Paris when the city initiated participatory budget for primary and secondary schools in its 2016 budget. Participatory budget of primary and secondary schools turned out to be an unquestionable success and still attracts huge interest[7]. Participatory budget in France is entirely optional.

In the French territorial self-government, participatory budget allows residents of territorial communities to freely submit proposals and constitutes a means of expression of their expectations and needs with regard to the quality of life, immediate environment, the future of their town districts and municipalities. Thanks to participatory budget, residents of territorial communities have a change to create their public space by putting forward motions and voting to select projects, which shall be carried out in their municipalities/departments/regions, and thus to contribute to improvement of their living conditions.

6 Sintomer and De Maillard point out that "*In all experiences of local participatory democracy, politicians and local government administrators regularly organise open neighbourhood meetings where they meet the citizens who want to take part. These meetings are organised from three to six times a year. Very often, they represent the main component of participatory democracy*". (Sintomer, De Maillard, 2007).

7 This practical exercise in democracy was made available to all schools and the participatory budget totalled 10 million Euro.

Pursuant to art. 211 item 1 and item 2 of the act on public finances of 27 August 2009, in the Polish legal order, the budget of a territorial-self-government unit is an annual plan income and expenses and revenues and expenditures, which is passed for a given budget year (Voivodeship Administrative Court in Gliwice: ref. no I SA/Gl 891/15).

Within the scope of these financial resources, a unit of territorial self-government may allocate a pool for execution of tasks proposed by residents. Responsibility to compile a draft budget and amendments falls solely onto the implementing body (Dolnicki, 2016: 215). Thus, residents cannot be granted competence via sub-delegation to amend the budget of a territorial self-government unit.

Within the French legal order, participatory budget also is a pool allocated from within the budget resources of a given territorial community. The budget is a basic financial act of a forward-looking and authorization nature, adopted annually. Legislative initiative with regard to the budget falls upon the executive body of a community, but the budget resolution is passed by the council of this territorial community. Draft budget includes expenses and incomes forecasted for the forthcoming year. The budget consists of income and expenses part, each of which includes two sections: "operational" **(**that is listing all the repetitive, regular expenses and incomes necessary for the ongoing operation of city services, such as employees' wages, maintenance of buildings, social assistance, etc.) and "investment" listing expenses and incomes that affect the assets of the territorial community (new buildings, development of schools, nurseries, renovation of sports facilities, housing projects, etc.). Participatory budget constitutes a predefined percentage of financial resources of the investment budget of a given territorial community (Nicoll, Muret,2014: 78). It must be pointed out that the income of a given unit, that is, the funds are obtained primarily from taxes. Such incomes supplement subsidies from the state (first and foremost, the so-called general subsidy – *dotation globale de fonctionnement*), other subsidies, operational income (e.g. income from use of sports facilities), loans, income from sale of city-owned real estate, however, sale transactions of real estates cannot be treated as investment income.

Within the Polish legal order, participatory budget covers tasks submitted by residents of a given community that fall within the catalogue of the unit's own tasks executed over a year-long cycle. Such undertakings should be of local or supralocal character, depending on what legal regulations stipulate. The catalogue of supralocal tasks includes such tasks that meet at least one of the following criteria:

- the tasks regard the needs of residents of more than one area of community;
- the place of execution of a proposed task is not assigned solely to a single auxiliary unit territory;
- the estimated cost of task execution exceeds the funds allocated to participatory budget of a given community territory (e.g. town district);
- the tasks must fit into the competences of the given unit's own tasks (Augustyniak, 2018: 382).

Within the French legal order, participatory budget includes two levels: a general community one (regarding e.g. the entire municipality) and district (covering a single town district council both that the arrondissement and quartier level). If the proposed task regards several town districts (e.g. the subject of the task covers fulfilment of the needs of residents of more than one district territory), such projects are often classified as city (municipal) one and not as town district ones. This is, however, a matter resolved by regulations of the organisation of participatory budget in a given municipality of town district. It must be also mentioned that participatory initiatives may be executed in schools as well, although such option aims at promoting citizenship within the school environment rather than creating a separate type of participatory budget.

Depending on local regulations in the form of resolutions of territorial community or town district councils (statutes or charters), we may identify certain elements shared by the submitted tasks for which funds are allocated within the budget of a given territorial community. These criteria will determine a certain degree of eligibility of a given proposal with regard to the basic formal and legal evaluation thereof. Thus, the undertakings presented in an application should present the characteristics of actions

for the public benefit (e.g. proposed transformations within public space – it is often emphasised that the proposals for participatory budget must be intended for use free of charge by all residents of a given town district or municipality) and fall within the scope of competences of a given community without any infringing its sole competence. What is more, these tasks should comply with legal regulations and should not be discriminating as well as they should match an investment outlay expressed as a percentage value predefined for a given territorial community (usually, 5 % of the investment budget of municipalities is allocated for participatory budget projects under one council term and circa 30 % of the town council budgets – arrondissement, with reservation that the projects should generate minimum cost of use).

3 Personal scope of participatory budget and procedures of its execution

3.1 Budget participants

Within the Polish legal order, the catalogue of entities entitled to participate and submit tasks for participatory budget include residents[8] of a given self-governing community. A task may also be submitted by a resident of a given municipality under the age of 18 years. Current trends in case-law of administrative courts show that "*the right to participate in social consultations on participatory budget is granted to every resident of a municipality. This means that the municipality council cannot define the minimum age giving the right to vote*" (Voivodeship Administrative Court in Opole: ref. no II SA/Op 109/18). Interference with the groups entitled to take part in such a form of social participation is unlawful. "*Restricting the group of persons entitled to participate in social consultations to residents of municipality over the age of 16 years constitutes*

8 Regulation of systemic acts do not define the term "resident of a territorial self-government unit", therefore, with regard to that matter, regulations of the Civil code must be applied. Thus, by analysing provisions of the Civil code, we must understand the term resident as a natural person with permanent residence within a given municipality (district, province – see art. 25 of the Civil code of 23 April 1963). This means that the consulted entity may be any resident of a given territorial self-government unit, regardless of their administrative or legal situation (national, foreigner, or a stateless person).

a serious breach of the law resulting in annulment of the contested order of the part in question" (Voivodeship Administrative Court in Poznań: ref. no IV SA/Po 176/18).

Pursuant to art. 5 a item 7 of the act on municipal self-government of 8 March1990, the municipality council defines through a resolution what requirements a participatory budget project shall meet, in particular, the required number of signatures in favour of the project, however, it cannot exceed 0,1 % of the total number of residents living in the territory covered by a participatory budget pool. Similar regulations were included in the act on district self-government of 5 June 1998 and the act on voivodeship self-government of 5 June 1998. So far, a definite number of residents were required for a task to be submitted for the budget (e.g. a minimum number of 10 people were required to support a submitted motion). A motion could also be submitted by other entities: auxiliary units, associations, non-governmental organizations, and other entities granted such right under resolutions of municipal councils.

The addressee of motions submitted by participants of the institution of participatory budget are the decision-making or executive bodies of territorial self-government units, which carry out initial formal and substantive verification of application in order to compile a list of projects out of which the residents will select their preferred ones through a popular vote.

However, an indirect form of participatory budget is also practised (the so called citizen request). Such an initiative consist in granting the residents the right to submit a motion proposing tasks regarding expenditures from participatory budget funds allocated to a given auxiliary unit (e.g. town district). In such a case, the addressee of such motion is the auxiliary unit authority and not the municipality. Such motions modify the budget of a given auxiliary unit, which constitutes a part of a municipal budget (Augustyniak, 2009: 218).

In the French Republic, any resident of a given territorial community, regardless of age and nationality, may participate in the participatory budget (Gaudin 2013: 96). This means that persons residing in a given municipality of town district permanently are allowed to vote if a two-level participatory budget is assumed within a given territorial community (e.g. municipality and town

district council). Therefore, within the French legal order, the scope of entities entitled to vote depends on internal regulations of participatory budget charters or regulations of town council charters. Voters select a pre-defined number of projects from a list for each level (municipal and town district). In the case of town district projects, every resident may vote in one town district only and this must be their district of residence or employment (the latter one is possible in the case of town district voting – arrondissement in Paris).

A motion may be initiated by a resident or a group of residents (usually, regulations and charts do not define any required number), associations, organizations operating within a given municipality or town district, and other entities. The addressees are bodies of territorial communities and bodies of town district councils. Within the French legal order, also an indirect form of participatory budget on town district council level (*arrondissement* – in Paris, Lyon, and Marseille) or town district council level (*conseil de quartier*) exists, but this form is voluntary, which means that each town district may or may not join participatory budget.

In most cases (both on the municipal and town district level), motions are submitted by uploading them on digital platforms of mayoralties. The authors of such motions need to provide their full name, address, date of birth, and e-mail address. For example, in Paris, the originators of proposals are identified on a digital platform s as residents or as representatives of groups and organizations (town district councils and associations in particular). Such data is then used for statistical purposes and presented by local authorities. Similarly, within the Polish legal order, proposals are most often submitted via online forms which include the petitioner's data and a description of the proposed task.

3.2 Stages of participatory budget – formal elements

Pursuant to systemic acts on self-government, the decision-making bodies of territorial self-government units define requirements to be met by a draft participatory budget through resolution. These may include, in particular

- formal requirements to be met by the proposed tasks;

- required number of residents' signatures in favour of the project, but the number cannot exceed 0,1 % of residents of the territory covered by the participatory budget pool for which the project is submitted;
- assessment principles of the submitted projects with regard to their compliance with law, technical feasibility, compliance with formal requirements, and the method of appealing if the project is excluded from voting;
- terms and procedures regarding the vote, determining the results, and disclosing them to the public, taking into consideration that the voting terms and procedures must ensure equality and proximity of the vote.

These are the obligatory elements, yet they do not exclude additional procedural elements compliant with legal regulations, which may be adopted by resolutions of the decision-making bodies. Taking the course of the consultative process in the form of participatory budget into consideration, we must conclude that each resolution defining the principles and procedures of execution thereof shall be classified as local legal act. In favour of such a statement is the provision of art. 5a of the act on commune self-government of 8 March 1990, which refers to the notion of resident as a consultative entity (Marchaj, 2018: 161).

Within the Polish legal order, the course in which residents execute their right to co-create the budget of a given unit may be divided into several stages. These are:

- submitting a task for financing (in the form of an application);
- pre-selection (formal and legal assessment) and substantive assessment of the motion;
- obtaining opinions and consultation (within the bodies of territorial self-government units);
- selecting particular tasks and compiling a ranking list of tasks by the unit's bodies for the residents' approval in the form of social consultations (through popular vote);
- introduction of a final list of tasks to be financed into the draft budget of a given unit of territorial self-government and execution thereof upon passing a corresponding budget resolution.

Further proceedings regard preparing a separate resolution signed by the presiding councillor and forwarding it to proper supervising bodies in order to launch the control and supervision procedure (Chojna-Duch, 2012: 456). During execution of participatory budget, a promotional and informational campaign should be carried out in order to inform the residents of the goal of that institution, encourage them to contribute actively, and promote information on the course and results of social consultations.

Within the French legal order, the council of a giver territorial community determines the funds within the scope of the investment budget to be allocated under a given term to finance projects selected by residents within the participatory budget. Town district councils (arrondissement) may also reserve a part of the local **(investment) budget to finance projects selected by residents within the scope of participatory budget executed within a given town district. Implementation of district** participatory budgets is based on contribution from district mayoralties, which play the role of local coordinators, especially with regard to provisions of regulations and charters adopted by town district councils.

Pursuant to legal regulations on the functioning of participatory budget in the French Republic (resolutions of municipal council, internal regulations and town district charters, as well as participatory budget charters), several procedural stages may be distinguished. The initial stage includes **rising the residents' awareness through** meetings and helping them to formalize their motions as well as launching an application platform. Before the budget procedure is started, so called field inspections (marches exploratoires), workshops, and sessions of round tables may take place. They are helpful in creating projects with contribution from residents, councillors, experts, and city services. The second stage consists in filing applications via a digital platform (online form) or sending hard copy applications to the mayoralty. During the third stage, the applications' eligibility is assessed. At this point in time, motions proposed by initiators of participatory budget are evaluated according to the following criteria: the projects' public interest, compliance with the law (all forms of discrimination are prohibited), correspondence with a pre-defined investment funds allocated to projects, matching the competences of a given community or district council. The authors

of applications which do not fulfil the basic eligibility criteria are notified of rejection and reasons for such a decision. At this stage, the scope of the project is also determined as city-wide or district-wide. The subsequent (fourth) stage consists in evaluation of projects by city services who formulate their opinion on the project's feasibility. Such an evaluation is related to the estimated cost of investment and its potential effect on expenditures. The results are usually published online, under a tab devoted to participatory budget. The fifth stage of the budget procedure consists in conducting public consultations **on the selected projects. This phase covers joint consultations and debate on the execution of these projects. In order to involve the residents at this stage, city services are obliged to make the list of projects available to** town district council and associations to enable their contribution into the debate on the projects, which may lead to improvement of individual projects or merging several ones. The sixth stage consists in selecting projects for popular vote**. Such a list is then published.** The final list of projects under the vote is approved by the district mayor form district-wide projects and municipal mayor for city-wide projects. The seventh stage consists in popular vote and announcing the winning projects. The vote is preceded by local information campaigns on the projects organized at both municipality and town district levels; public meetings and thematic committees are initiated in order to present the projects with participation of associations and other pro-social organisations operating within a given district. Two forms of vote are permissible: electronic and traditional, by means of ballot-urns placed in municipal or town district mayoralty and other designated locations. The voters select a pre-defined number of projects from a list for each level – municipal and town district. All residents of a given municipality are allowed to vote (regardless of their age and nationality). In the case of district-wide projects, each resident may vote in one district only depending on their place of residence or employment. The results are calculated separately for the municipality (city) and each individual district taking part in the participatory budget. At both levels, projects scoring most votes within the limits of a budget pool pre-defined for each level are selected. The final stage consists in voting on the budget at sessions of municipal/town district councils (arrondissement), with

consideration for priorities put forward by residents under the participatory budget. The residents are usually informed of the voting results on projects selected for participatory budget in December of the year in which they participated in the participatory budget procedure since this is the time when municipalities pass their budgets. The final, eighth stage consists in providing the residents with ongoing information, via e-mail or a dedicated website, on implementation and execution of proposals selected through popular vote. Reports on execution of proposals within participatory budget are presented annually at a session of the municipal council. District-wide proposals are reported in similarly at a session of town district council. All reports on district-wide proposals, submitted to district councils, are presented annually at a municipal council session. It is a common practice to place a logotype or inscription visible within the public space to indicate that a given project resulted from cooperation with residents of a local community within the scope of participatory budget.

4 Conclusion – direction of changes

Within both legal orders, the institution of participatory budget must be perceived as an important element of the development of Civil society, which guarantees the residents of communities participation in making decisions on their own matters as an expression of better management of public funds. It is an efficient tool for stimulating the activity of residents of territorial self-government unit and an expression of self-governance. Participatory budget "*appears to be a particularly significant innovation as it refers to the most meaningful decision-making process – allocation of local government's expenditure*" (Sześciło, 2015: 385). In general, participatory budgeting programs are a relatively a new institution both in Poland and French economy and in the legal field. "*We should evaluate their implementation positively and note the need for their further development*" (Mironova, Kozlova, 2018: 230).

Granting the residents the right to propose one-year tasks financed from the budget of a given unit does not raise legal doubts. It is an instrument for execution of the subsidiarity principle defined in the preamble to the Polish Constitution and in provisions of the European Charter of Local Self-Government.

In France, the institution of participatory budget is regulated either by the provisions of internal statutes of municipal councils (or town district councils – *arrondissement*), town council charter, or participatory budget charter. On the other hand, since 1 January 2019, within the Polish legal order, participatory budget has been regulated under systemic acts on self-government and resolutions of decision-making bodies of territorial self-government units.

Both within the Polish and French legal order, two types of participatory budget may be distinguished: community-wide and district-wide, with the reservation that in France children and young adults are actively involved in managing participatory budgets allocated to their schools.

Both Polish and French procedure is divided into several stages (from an information campaign, submitting a proposal, preselection, formal, legal, and substantive verification, through compilation of a ranking list, final vote, and introduction of the winning project into the budget of a given unit/community).

Within the French legal order, a lot of pressure is put on information and consultation policies within participatory budget. Numerous meeting are held prior to, during verification of the projects and prior to the final vote to stimulate active involvement of residents, associations, and other entities. Municipal authorities and town district councils invite the residents to co-create projects regarding a given location or a given thematic area. They organize, on city and district level, workshops on co-creating projects in order to achieve a collective character of the works aimed at defining a common vision for local public space. In Polish editions of participatory budget, information and consultation campaign also plays an important role, but not as important as could be. It must be concluded that, in most cases, there is a lack of consultation and joint attempts (at municipal or auxiliary unit level) enabling merging projects already included in the ranking list, which is not, in fact, consulted nor discussed with residents again, but forwarded directly to the voting stage. An increase of the residents' involvement into the information and consultations campaign at every stage of the participatory budget procedure is thus desired.

Undertakings carried out within the scope of participatory budget should be of local or supra-local nature (depending on applicable regulations), comply with legal regulations, fit into the competences of public authorities and fall within the range of amounts defined in the budget.

Introduction of legal regulations, which would enable residents to appeal to the administrative court if bodies of local self-government fail to act on such initiative, should be considered. It seems necessary, in order to improve the operation of the instrument, to launch judicial review on that matter.

Participatory budget should also be based on open and modern methods of decentralized management, as an expression of trust in residents of a self-governing community. It is aimed at strengthening the bonds between citizens, institutions, and their representatives, ensure a higher degree of transparency in public finance management, help in developing pedagogy of public activity, and utilize the residents' knowledge and creativity. Experiences related to participatory budget in Poland and in France show that it is an excellent example of the immediate democracy (*démocratie de proximitê*), which consists in ongoing debate with representative democracy, transgressing the boundaries of public decisions, and redefining the distribution of power between the representative and direct democracy (Gret, Sintomer, 2005: 133).

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Selected Questions in Development of Financial Activity of the State and Municipal Units

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Abstract

The study is devoted to issues related to the financial activity of the state and municipal unites, to the use of public finances as a regulator of public relations. The main objective of this study is to clarify the current content of the financial activity of the state and municipal unites as a category of financial law, defining its role in legal theory. Relationships and interdependencies with public finances are considered. Using analytical, systemic, comparative legal and formal logical methods, the study substantiates the relationship and interdependence of the science of financial law with the economy, political and social life.

Keywords: Financial Activity of the State and Municipal Unites; Public Finances; State Finances; Local Finances; Budget; Financial Law; Financial and Legal Mechanisms; Taxes.

JEL Classification: O17.

1 Introduction

The main problems in the financial activity of the state and municipal unites are well known to everyone. Increasing tax burden, wage and social security stagnation, regional differences in budget and financial opportunities, uneven economic development, increasing differences in the standard of living of the population, as well as legality, expediency and efficiency of using public finances – all these topics constantly attract the attention

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of common citizens, as public service users, as well as scholars, practitioners, politicians and businessmen. The purpose of this study is to clarify the current content of the financial and legal institution called "financial activity of the state and municipal unites" in conjunction with the category of public and local finances, to determine their role and importance in public law theory and practice. The author believes that the application of the package scientific approach to the study of this social phenomenon in conjunction with the economic, political and sociological sciences allows, through the lens of this public category, to evaluate the practice of implementing other financial and legal mechanisms and categories. The author is confident of the advantage of historical, comparative methods in financial and legal research. With their help, as well as analytical, system based, formal-logical methods in the study it is substantiated that the financial activity of the state is primary in relation to other financial institutions that arise as a result of its implementation. The study confirms the theoretical significance of financial activity as a methodological tool used in the development and formation of the theory of financial law. According to the author, the nature of the financial activity of the state does not allow investigating it only in a legal aspect. Without a connection with economic and political science, it is impossible to establish as well as to understand, why wonderful financial laws remain a declaration, and our standard of living and the economy are at a standstill. The use of a package or "joint" approach possible within the framework of financial law, i.e. the analysis and evaluation of financial phenomena and financial and legal mechanisms that ensure them, through the prism of financial science, political science, sociology and economics, in our opinion, provides an opportunity for deeper scientific knowledge and meaningful enforcement.

2 On the essence, interrelations and interdependencies of the financial activity of the state

The financial activity of the state, and nowadays, of municipal unites as well, traditionally refers to the key concepts of financial and legal theory. It happened that in the science of financial law, and, consequently, in textbooks,

the presentation of the content always begins with the concept of financial activity of the state. Note, so far, the discussion about the nature, role, and forms of state financial activity has not been closed in modern legal science. In this regard, using historical and comparative methods, let us consider the concept of state financial activity and try to explain the need for new approaches to understanding its role in financial law and government. For the first time, in the Russian science of financial law, the phrase "financial activity of the state" appears in the well-known financial scholar, from St.-Petersburg University V. A. Lebedev, who viewed it in conjunction with the organization of state satisfaction and the financial power of the state. He singled out two of its forms: public, purely state, related to the financial organization of the state, the budget sphere and control over the state economy, and private, contractual – with respect to fiscal transactions of individuals with the treasury. (Lebedev, 2000: 135–136) Currently, the opinion of Lebedev on the financial activity of the state as dualistic can be proceeded. Because of its implementation, the state uses public law and private law methods of influencing social relations in the financial sphere of the economy. Moreover, in this regard, in modern Russian science of financial law, the public financial activity of the state is absolutely fairly defined as the sphere of financial and legal regulation. (Karaseva, 2012: 28)

On the contrary, in the Soviet financial and legal science, it was primarily about administrative and legal regulation. In the course of financial activity, the state, acting as the organizing element of economic and economic life, administratively influenced the economy. Of course, as a kind of subjective activity as follows from its content, the financial activity of the state is primarily determined by the level of socio-economic development of society, its needs, the status of the state and the prevailing belief system in society. Therefore, the views of scientists on the category of the financial activity of the state are not constant, and are not due to their subjective wishes, but to the objective circumstances of social development.

The state, in the course of financial activity, carrying out the functions of creating and distributing monetary funds and public financial resources, declares the goal of ensuring the satisfaction of the "collective, public" needs of society. This is so important and institutional for society

that the financial activity of the state is in practice quite naturally transformed into a completely independent direction of state policy. The change in the economic structure, the transition from a socialist economy to a market economy opened up opportunities for the involvement of private finances in the sphere of public interests, the delegation of public authority to private entities (for example, to banks, state corporations, other business corporations). Thus, the trend of combining the interests of the state and business contributes to the expansion of the sphere of financial activity of the state. Here it is necessary to wholeheartedly agree with the opinion of S. V. Zapolsky that "*the financial activity of the state (and in the works for 15 years in a row, the similar activity of the municipal unites is definitely highlighted) is precisely the mover who launches in one form or another the effect of tax, budget, foreign economic, insurance and many other specific financial arrangements. Overall, the financial activity of the state is implemented sovereign measure of the government in respect to specific financial and legal institutions*." (Zapolsky, 2010: 75)

Modern reality, in connection with the combination of the interests of the state and business, poses the state the problem of expanding the boundaries of financial activity, removing restrictions on the use of state and municipal finances. In this regard, the main aspect, in our opinion, is the question of strict respect of public interests.

The financial activity of the state as a subject of public authority is always public and is carried out exclusively in public law forms. The financial activity of the state differs from the financial activity of other subjects by these two characteristics. These properties of the financial activity of the state were identified and described in 1960 by a prominent theorist of Soviet financial law, E. A. Rovinsky. "*The financial activity of the state are lawful actions of state bodies aimed at mobilizing, distributing and using by the Soviet state the financial resources that form part of the national income of the USSR and form Therefore, the financial activity is a special type of state activity, where the monetary relations are forms and these relations regulated by financial law*." (Rovinsky, 2017: 23) Subsequently, leading experts of Russian financial law successfully developed the hypothesis of financial activity by the state as a carrier of public authority in the course of performing specific functions. "*Through financial activity, a material basis is created, which is necessary for the functioning of government bodies and authorities, law enforcement*

agencies, ensuring the defense capability and security of the country." (Khimicheva, 2003: 38). Exploring the nature of this phenomenon, E. Sokolova believes that "*by the financial activity of the state should be understood a special type of state activity, expressed in the implementation by the state bodies… of organizational, legal and actual actions aimed at creating, distributing (redistributing) and using funds of financial resources, both centralized and decentralized, necessary in the conditions of market for financial support of the life of society and the state*". (Sokolova, 2008: 14)

Analysis of the definitions of the concept of the financial activity of the state allows us to assert that the financial activity of the state is not only a special type of state activity, but is also a means of achieving the goals set by the state or local government. In the construction of most of the definitions of this concept, the managerial aspect is clearly visible. This very aspect determines the binding nature of the goal for any act of the state or municipality in the field of finance. In this regard, we can also divide the hypothesis of S. Zapolsky that "*fundamentally, the financial activity of the state should not be considered as a legal category, it is rather a method of political integration of various means of influence of the state on financial phenomena and processes*". (Zapolsky, 2010: 75) It should be noted that theorists of the Russian financial law O. Gorbunova and M. Karaseva have already noted the coincidence of the financial activities of the state and municipalities with their management activities. (Gorbunova, 2012: 72–77), (Karaseva, 1999: 18–19)

The problems of the society, its development, first, are solved in the course of the financial activity of the state or municipal unites. At the same time, public relations that are formed in the process of financial activity by the state and municipal unites are subject to financial law. Earlier, we noted that, by its nature, this activity is always of managerial type, that is, carried out by authorized bodies; legal, i.e. always has a regulatory basis; property, as associated with the formation, redistribution and use of cash funds. These characteristics of the financial activity of the state and municipal unites are important for further research of this financial and legal category and socio-economic phenomenon.

In connection with the transition to a market economy, the role of the state and municipal unites in the regulation of public monetary funds, their accumulation, distribution and use, compared with the Soviet economy, has

changed significantly. Finances still fulfil the role of "interconnecting vessels" in the economy; as the result of this activity, national income is still being redistributed, but a new connection has emerged between centralized public finances and decentralized private ones. Thus, the function of redistributing of the part of the national income in the structure of financial activity has significantly strengthened the managerial component with a complex system of goal setting. The state and the municipal unites seize from the individuals part of their personal income in the form of taxes and fees in order to ensure its own uninterrupted functioning and satisfaction of public needs. These goals involve the use of public finances, that is, state and local. Any activity in the state or at the local level requires the redistribution of finances, and such redistribution is carried out in the course of financial activity. In the Russian science of financial law, it is proved that the finances used in the process of financial activity fully reflect all the processes occurring in the economy, social development, politics and in public moods. Any event in the state cannot be held without the redistribution of financial resources, that is, without the financial activity of the state and local authorities (Gorbunova, 2017: 341).

Summarizing the views of the Russian financial and legal theory, we can conclude that the financial activity of the state and municipal unites, as a theoretical concept is a legal category, on the contrary finances are an economic category. In Russian economic theory, finances do not mean the money itself, but the relationship between people about the formation, redistribution and usage of funds of financial resources. Finances serve as an economic tool for the distribution of gross social product and national income. (Rodionova, 1993: 11–12) In this regard, for the purposes of our research, the opinion of E. Sokolova on determining the structure of the financial system seems to be very interesting, its basis would be determined by the form of ownership of the respective funds of funds. Based on the provisions of Article 8 of the Constitution of the Russian Federation, the financial system is represented as a set of four links or institutions: government finances, local finances, private finances and other finances, the latter classifies the deposit insurance funds of citizens (Sokolova, 2006: 17–19). These provisions of the domestic financial and legal theory allow us to hypothesize that in the course

of the financial activity of the state and municipal unites carried out within the financial system, public finances interact with local, private and other finances, thus creating various interdependencies in the state and local territories, economy, politics, social life. Through the financial activity of the state and municipal unites as a type of state activity, financial power is exercised and direct state and municipal management of all spheres of public life is exercised. Thus, the financial activity of the state and municipal unites we define as: 1) a financial and legal category, and it is possible to evaluate other financial and legal institutions and categories, to form financial and legal mechanisms through the prism of this category; 2) financial and legal institution, defining the boundaries of the subject of financial law; 3) a legal phenomenon integrated into the socio-economic life of society, allowing for the management influence of the state and local authorities on various social processes; 4) form of management. We intend to develop this opinion in further studies that will be connected with the formation of a system of goal setting and mechanisms for ensuring public interests.

3 The value of financial activity in foreign financial and legal theory

We should note that in Western European financial and legal theory, which is economic in its content in comparison with Russian, and Russian, the state finances as an object of financial activity that is the subject of financial law are initially considered in their dynamics, that is, in the process of financial operations, the object of which they are. Thus, the study of the functions performed by state finances, the conditions in which these functions are carried out, the consequences that appear in political and economic life, is one of the most important aspects of research in the field of financial law. That is the position of the hard-liner on Western European financial law, Paul Marie Godmet. (Godmet, 1978: 41–43)

For our research, the positions of Czech financial and legal theorists are of particular interest. Interesting is the view of Peter Mrkývka on the category we are examining. Mrkývka considers financial activity as a certain way of material support by the state for the performance of its functions. In order to meet the need to have the necessary financial sources

and resources, the state in an authoritative way accumulates the funds received from the sale of products of production and services, and then redistributes them. Such activity is defined in the Czech financial and legal theory as the financial activity of the state and denotes the accumulation of funds in centralized and decentralized cash funds, and their subsequent distribution in the financial market. An example of a centralized fund is the state budget, and an example of a decentralized fund is the budget of settlements, and other territorial administrative units. Mrkývka rightfully believes that the financial activity of the state is carried out using various methods, and classifies these methods based on specific methods of accumulation and distribution, or the use of funds into two groups: (1) the mobilization methods like the creation of funds and the creation of monetary reserves, and (2) the implementation methods like distributing of monetary resources and funds. (Mrkývka, 2016: 51–52) At the same time, another classification is proposed in the Czech financial and legal theory. Milan Bakeš, using the principle of monetary funds' creating, distributing and using, identifies four methods of financial activity: the non-refundable method, refundable method, insurance method, implementation method. (Bakeš, 2012: 10–11)

M. Karfíková considers the financial activity of the state as an activity of creating, distributing and using funds at the level of separate economies. Depending on the type of entity involved in this activity, as well as on other specific features of this activity, there are financial activity of social and legal corporations, in particular, the state and territorially autonomous units, financial activity of business persons, in particular business corporations, individual entrepreneurs and financial activity of non-profit persons, in particular households. Karfíková, like in the Russian financial and legal theory, very closely correlates financial activity with the creation and sale of gross domestic product, with its distribution and redistribution in monetary terms. (Karfíková, 2018: 5–6) Thus, the author identifies the property nature of financial activity, manifested through money, acting in its function of the universal exchange medium or the universal means of payment.

Financial activity in the broad sense of the word, in Czech financial and legal theory also includes activities that are not directly related to real money turnover and monetary transactions. That is, when the creation, distribution

and usage of monetary funds are only planned, foreseen or assumed, or on the contrary are described, investigated and evaluated retroactively. This applies to almost the entire field of financial planning, for example, the preparation of draft state budgets or local budgets, financial relations within the framework of financial statements, control over the management of public funds. Although in these cases we are not talking about a direct relation to the financial resources that constitute public monetary funds, one can always find such an attitude, at least indirectly. Projected onto Russian financial and legal theory, this aspect of financial activity is procedural and relates to the budget process.

Karfíková proposes to classify financial activity in various categories, among which she highlights the classification based on the economic sectors of the national economy where financial activity is carried out, and then depending on the type of persons or other units that carry out financial activity. The most common division of the economic sectors of the national economy, into two main sectors, namely the public sector and the private sector is used here. The financial activity of the public sector primarily includes the financial activity of the state and public authorities and administration, and then the activity of autonomous territorial units and local authorities and administration, as well as the activities of other social and legal entities. Within the framework of the financial activity of the public sector, in most cases financial relations arise that constitute the content of the concept of "public finances". In the Czech financial and legal theory, the very concept of "public finances" is considered, and it includes part of the monetary relations concerning the state budget and local budgets, state trust funds, state and local units, in particular subsidized organizations or organizational components of the state and territorial autonomous units, public schools and public research institutions. (Karfíková, 2018: 5–6) Please note that this concept in the Russian scientific theory is similarly considered by economic theory.

In contrast to the Russian financial and legal theory, the Czech doctrine distinguishes the financial activity of the private sector, and it uses and distinguishes a subdivision the financial activity of the non-business sector, namely societies and households, and the financial activity of the business sector, including trading corporations, entrepreneurs and other types

of business units. The banking sector or the insurance sector stand out the financial activity of specific sectors of financial institutions in the same framework. The financial activity of these sectors includes financial relations related to the components of private finances, as well as the finances of enterprises, household finances, bank finances, and insurance companies' finances. In the Russian financial and legal theory, such a unit takes place, but within the framework of the financial activity of the state and municipal unites, these resources are considered as involved, or drawn in the general financial system in achieving of public goals. If this moment is absent, then this financial activity is considered outside the scope of financial law.

Membership in the European Union leaves a definite mark on the development of national financial law. Karfíková notes that from the point of view of the territorial distribution of the power of financial activity and its impact on public finances, one should also distinguish between national financial activity and international financial activity. National financial activity represents domestic financial activity, and international financial activity, respectively – external financial activity. The outstanding feature of international financial activity lies in the fact that within it the financial relations between units of different national economies mainly arise, terminates, and replace each other. At the same time, cash funds created from cash in foreign currencies are also being created and being used. Recently, supranational financial activity has been added to the above-mentioned categories of financial activity, it is characteristic of the supranational group of states that have number of powers in the field of public finance in the interests of a group of states. A typical example of such a group of states is the European Union.

Summarizing, in our opinion, both in foreign and domestic financial and legal theories, there is a clear interconnection between the financial activity of the state and municipal unites and public finances, which directly determines their interdependence. On the one hand, public finances are completely in the will and disposal of state and local authorities, and on the other hand, their volume determines the level of financial activity of the state and local authorities, the degree of their influence on the economy and society. Obviously, in the course of financial activity of any kind

of implementation, the management function is translated into practise with the help of money. In financial and legal theory, it has long been noted that management through finances is the most effective regulator of social relations. By directing cash flows to form monetary funds, which are later used for the needs of society, the state thus stimulates, or, conversely, restricts activities in certain areas. Finances, in addition, are the best information source. Insufficient budgetary provisions of one or another types of human activity leads to their curtailment, as well as to other negative phenomena. (Gorbunova, 2007: 7) In the aggregate consideration of the categories of financial activity and finance, despite their belonging to various sciences, law and economics, the relationship between the science of financial law and economics, political science, and sociology is most clearly revealed. Professor Kristina Piotrovska-Marchak, in this regard, notes the phenomenon of the coverage of a particular field of study in several sciences of various scientific disciplines or fields. This can be fully attributed to the subject of this study – the financial activities of the state and municipalities. The professor writes that this hypothesis concerns the area of knowledge for which money is a discriminant. Financial phenomena and processes are a field of scientific discipline, such as finance, which is suitable for the field of economic sciences and law. In the second case, a part of the right is called financial law (Piotrowska-Marczak, 2018).

This issue is important for substantiating an interdisciplinary approach to economic, financial phenomena, their joint research and systematization of knowledge about them in the framework of both sciences. We consider it necessary to note that for the time being, relations and dependencies of economic, financial and legal theory with political science and sociology remain unattended. By systematizing the knowledge of the studied questions, it is possible to establish the interrelation of other categories of these various sciences. For example, the following financial and legal and economic categories: "taxes" and "economic growth", "indirect taxation" and "economic conditions", "budget deficit" and "inflation".

It is important that the relationship entails interdependence, that is, the possibility of a specific financial and legal instrument influencing specific economic, social and political processes. The connection of financial law with

economics in turn contributes to a deeper knowledge of financial phenomena and the identification of patterns. Systematization of knowledge about the relationship between economic and financial-legal science allows you to conduct more detailed studies of certain phenomena, identify the causes of their ineffectiveness, influence them, change and regulate.

It should be noted that at all times and in all socio-economic formations, public finances were a significant regulatory tool of social relations, a means of government. The significant importance that public finances have in the life of any modern society determines the importance of legal regulation of relations connected with their formation, distribution, use, financial operations with their participation, the organization of their administration and control. These relationships are traditionally governed by financial law.

It is noteworthy that it is similarly possible to establish the relationship between other categories of these various sciences. For example, the following financial and legal and economic categories: taxes and economic growth, indirect taxation and economic conditions, budget deficit and inflation. It is important that the relationship create interdependence, that is, the possibility of a specific financial and legal instrument influencing specific economic, social and political processes. The connection of the science of financial law with economics in its turn contributes to a deeper knowledge of financial phenomena and the identification of patterns. It should be noted that both now and always and in all socio-economic formations, public finances were a significant regulatory tool of social relations, a means of state administration control. The significant importance that public finances have in the life of any modern society determines the importance of legal regulation of relations connected with their formation, distribution, usage, financial operations with their participation, and the organization of their administration and control. These relationships are governed by financial law.

However, without its relationship with financial, economic science, its regulatory capabilities are reduced. The modern theorists of Czech financial law have repeatedly written about the evolution of financial law in this aspect. Professor M. Karfíková in her work notes that financial relations, financial activity of the state, finances, financial system should not be considered

outside the relationship of financial and legal science. These phenomena are interrelated and interdependent, which, in turn, determines the evolution of modern financial law in the direction of the development of an interdisciplinary approach (Karfíková, 2015).

4 Conclusion

The presented study is an attempt to fragmentarily reflect the current state of theoretical views on the financial activity of the state and municipal unites in Russian and foreign financial and legal doctrine. It should be noted that throughout the categorical financial and legal apparatus the theoretical value of this concept is universally recognized.

The traditional approach of considering this category as a financial and legal institution does not meet the modern needs of organizational and legal support of social relations.

Financial activity has obviously gone beyond the boundaries of public finances, moreover the finances and other forms of ownership are actually involved in it.

Using finance in the course of financial activities, the state and municipalities regulate social relations and influence our lives.

This is obviously the most important institution of financial law, but its significance is much wider and probably requires an interdisciplinary approach. We represent in its historical development, and at the same time, we did not confine ourselves to modern Russian legal theory. The use of public finance in financial activity, finances as a whole, determines the close interconnection and interdependence of these phenomena and presupposes relations and dependencies between economic and financial-legal theory.

The financial activity of the state and municipal unites is a single holistic economic and legal phenomenon, a kind of social phenomenon that develops dynamically.

The financial activity of the state and municipal unites is a type of power activity of the state and local government, carried out in the process of managing public relations through finances.

The financial activity of the state and municipal unites generates such social relations that fall within the scope of regulation of financial law.

The financial activity of the state and municipal unites has in itself an internal contradiction of the public interests of society and the accumulated financial resource (budget).

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Challenges in the Public Financial Management and Control of Territorial Self-governing Units

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Abstract

This contribution deals with issues related to the financial management and control system of territorial self-governing units especially with regard to the proposed extension of the Supreme Audit Office competences. The aim of this paper is to verify the hypothesis that the proposed extension of the Supreme Audit Office's supervisory competences to territorial self-governing units in the Czech Republic will increase the effectiveness of the protection of public funds.

Keywords: Financial Management and Control; Supreme Audit Office; Territorial Self-governing Units; Public Funds.

JEL Classification: H21; H77.

1 Introduction

One of key legislative proposals discussed in the Chamber of Deputies of the Czech Republic is undoubtedly an amendment of the Act on Extending of the Supreme Audit Office Authority (Parliamentary prints no. 229, no. 230 and no. 360). One of the fundamental changes, that it should bring, is the introduction of further audit activities on the financial management of territorial self-governing units. Although the financial management and control of territorial self-governing units is up-to-date issue for the central state administration bodies, associations of territorial self-governing units and both chambers of the Parliament of the Czech Republic, this topic is unjustly neglected by the scientific community. This proves in particular by the lack of a theoretical-legal basis, which is crucial for the upcoming legislative changes.

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The aim of this paper is to verify the hypothesis that the proposed extension of the Supreme Audit Office's supervisory competences to territorial self-governing units in the Czech Republic will increase the effectiveness of the protection of public funds. In particular, methods of analysis, comparison and induction are used. First, the object and scope of the existing control system of territorial self-governing units is analyzed. Individual types of control activities are compared. Used comparative criteria are the object and scope of the management and control, state administration authority, the frequency and procedural adjustment. In the same way, the proposed extension of the Supreme Audit Office's competences is analyzed by the same criteria. Subsequently, a general conclusion in relation to the hypothesis set above is made by using the analyzed details.

2 Management and control of territorial self-governing units

The basis of the existence of territorial self-governing units is laid down in Act No. 1/1993 Coll., The Constitution of the Czech Republic, as amended (hereinafter referred to as the "Constitution of the Czech Republic"). The chapter seven of the Constitution of the Czech Republic is devoted to territorial self-governing. Article 99 divides territorial self-governing units into basic ones, which are municipalities and higher ones, which are regions. Regarding the aim of this paper Article 101(3) of the Constitution of the Czech Republic is important. It stipulates that territorial self-governing units are public law corporations which may own property and manage their affairs on the basis of their own budget. This is a rule that does not substantially deviate from the European average. However, territorial self-governing units in the Czech Republic has significant specificities that distinguish them from territorial self-governing units in other European countries and which cause many problems that municipalities and regions in the Czech Republic face. The main problems are great fragmentation of territorial self-governing units and the size of municipalities (which is still being discussed) and the size of regions (which, for the time, is unnoticed by the lay and professional public).

In this context, the OECD study (Economic Overview of the Czech Republic) points out that the size of municipalities in the Czech Republic is the smallest in the OECD countries and the regions are the seventh smallest. Roughly three quarters of municipalities have less than 1000 inhabitants and a quarter of them have less than 200 inhabitants. At the same time, a number of them, in addition to ordinary self-governing tasks, also carry out tasks within the so-called delegated competences, i.e. tasks of the state administration. The size of municipalities, the tasks they provide and the high degree of deconcentration are also reflected in the way of financing. The primary source of income, under Act No. 243/2000 Coll., On Budgetary Determination of the Revenues of Certain Taxes to Territorial Self-Governing Units and Certain State Funds (the Act on Budgetary Determination of Taxes), as amended, are tax revenues that are managed and selected at national level. Despite this, the prevailing view is that state control (audit) of the territorial self-governing units is an interference with their right to self-government (Parliamentary print no. 229, no. 230 and no. 360).

Regarding management and control activities performed by the state, the essential provision is the Article 101(4) of the Constitution of the Czech Republic, which states: "The state may intervene in the affairs of territorial self-governing units only if such is required for the protection of law and only in the manner provided for by statute." Management and control of territorial self-governing units is performed from the level of several state control authorities, according to several legal regulations, i.e. with different objectives and by different procedural rules. Regarding the protection of public funds, the fundamental control activity are the management and control of independent self-governing competence, the financial management and control review, the management and control of public financial subsidy, the recipient of which is the territorial self-governing unit and the internal management and control system. In addition to these control activities, there is, of course, other which, however, cannot primarily be regarded as controls (audits) aimed at protecting public funds. These include, for example, control of the performance of state administration by municipalities and regions, control by the Office for the Protection of Competition, the Office for Personal Data Protection, and by the Labor Office.

2.1 Management and control of independent self-governing competence

The Ministry of the Interior is entrusted with the management and control of independent self-governing competence of municipalities and regions. The substantive legislation is governed by the provisions of articles 129 and 129a of Act No. 128/2000 Coll., On Municipalities (Municipal Establishment), as amended (hereinafter the "Act on Municipalities"), articles 86 and 87 of Act No. 129/2000 Coll., On Regions (Regional Establishment), as amended (hereinafter the "Regions Act") and articles 113 and 114 of Act No. 131/2000 Coll., On the Capital City of Prague, as amended (hereinafter referred to as "the Capital City Act ").

Its aim is to verify whether territorial self-governing units comply with the legal regulations with the exception of civil, commercial and labor law. An exemplary list of the independent competence of territorial self-governing units is governed by the relevant laws (articles 84, 85 and 102 of the Municipalities Act, articles 11, 35, 36 and 59 of the Regions Act, articles 59 and 68 of the Capital City Act). These include development activities, education, health care, cleaning and maintenance of roads and greenery. From the point of view of the protection of public funds, this mainly concerns the control of legal acts in the management of municipal property or the control of the remuneration of councilors. It follows from the definition of the control that its object is wider than just the protection of public funds and, on the other hand, it the financial management and control is not fully included. In most cases, management and control of independent self-governing competence is initiated by civic initiative (Analysis of the Ministry of Finance, Evaluation Report of the Ministry of Interior) and does not have a character of regular or periodic control activity. The control procedure is regulated by Act No. 255/2012 Coll., On Control (Control Code), as amended (hereinafter referred to as the "Control Code").

2.2 The financial management and control review

The financial management and control review of territorial self-governing units is a periodic inspection, which is carried out every year according to Act No. 420/2004 Coll., on The Financial Management and Control

Review of Territorial Self-governing Units and voluntary association of municipalities, as amended (hereinafter referred to as the "Review Act"). For the purposes of the Review Act, the abbreviation "Territorial Unit" is introduced, which, in addition to the basic territorial self-governing units – municipalities and higher territorial self-governing units, includes the city districts of Prague, regional councils of Cohesion Regions and voluntary unions of municipalities. This is an interesting construction that is, but from the point of view of this article, irrelevant.

The financial management and control review of municipalities is carried out by an auditor registered in the Chamber of Auditors of the Czech Republic or a Regional Office as a delegated state administration. It is up to the municipality to decide whether the review will be carried out by the Regional Office or the auditor. The City of Prague may choose between an auditor and the Ministry of Finance. Regions are always reviewed by the Ministry of Finance. The key point is that the auditor does not have the status of a supervisory (state) authority when carrying the review, i.e. it is not a standard delegation of competences of a state administration authority to a private entity. This difference is most noticeable when the findings of the review are transmitted to the authorities that have the competence to conduct administrative or tax proceedings and, where appropriate, to impose sanctions. The obligation to transmit the findings to the administrative authority for follow-up proceedings arises from article 25(4) of the Control Code and applies only to supervisory (state) bodies. The significance of this specific role of the auditor is also given by the fact that the auditor is mainly recruited by the largest municipalities in the Czech Republic (Information of the Ministry of Finance) as the costs of the audit are paid by the municipality. The costs of carrying out the review of management by the regional authorities and the Ministry of Finance are always borne by the relevant supervisory (state) authority.

The object of the audit is the management and control of the territorial self-governing unit for the financial year, which is further specified in article 2 of the Review Act. In addition to checking compliance with legal regulations, management and control are also reviewed from other aspects defined in article 3 of the Review Act. Despite explicit reference

to budgetary compliance or the factual and formal correctness of documents, this is essentially a verification of compliance with the law, i.e. similar to the definition of management and control of independent self-governing competence. In addition to the verification of compliance with legal regulations, the provisions of article 3 letter (c) states, the other criteria – compliance with the purpose of the subsidy or repayable financial assistance and the conditions for its use. In this case, compliance with the decision, possibly with the public contract on the provision of a subsidy or repayable financial assistance, will be verified.

The control procedure is regulated by the Control Code and special rules defined in the Review Act.

2.3 The management and control of public financial subsidy

Public financial subsidy is defined in article 2 letter j) of Act No. 320/2001 Coll., on Financial Management and Control in Public Administration and on Amendments to Certain Acts (Act on Financial Management and Control), as amended (hereinafter referred to as the "Financial Management and Control Act"). In addition to subsidies sensu stricto, the term also includes contributions, repayable financial assistance and other resources provided from public budgets and less used forms of support such as state guarantees or tax exemptions. The competences of entities to carry out financial management and control of public financial subsidy are regulated in articles 7 to 9a of the Financial Management and Control Act. Applicants and recipients of public financial subsidy are verified by the Ministry of Finance in addition to the provider and, in the case of public financial subsidy from the budget of the European Union, also other entities of the implementation structure (e.g. paying agency) and EU institutions. This control activity is called public administration control. The Financial Management and Control Act also entrusts competences to carry out public administration control to tax authorities, which, however, do not actually exercise it.

The object of the public administration control is primarily the conditions under which public financial subsidy was provided. The conditions are set out in the relevant grant decision or public contract for the granting

of public financial subsidy and in legislation (e.g. public procurement legislation) or other documents (e.g. operational program terms). The procedure of public administration control is governed by the Control Code except for minor differences (article 13a of the Financial Management and Control Act) defined for the audit performed by the Audit Authority on funds from the European Union budget (in the Czech Republic the competence of the Audit Authority is performed by the Ministry of Finance).

Furthermore, the recipient of the public financial subsidy is verified by the tax authority as part of the tax audit. This is due to the fact that the payment for breach of budgetary discipline (the return of public funds back to the public budget if the recipient of public financial support does not comply with the stipulated conditions), falls within the tax administration and competences of tax authorities (see Article 44a of Act no. 218/2000 Coll., on budgetary rules and amending certain related acts (the Budgetary Rules Act), as amended). For the sake of completeness, it should be added that this competence of tax authorities only applies to public financial subsidy provided from the state budget and the budget of the European Union. The object of tax audit is de facto identical to the object of public administration control, only the procedure differs.

The procedure of tax audit is regulated by Act No. 280/2009 Coll., The Tax Procedure Code, as amended (hereinafter referred to as the "Tax Procedure Code"). In this case, the question is what should be the objective of a tax audit in the context of the management and control of public financial subsidy when the tax audit is carried out in the context of tax administration. The objective of the tax administration is defined in article 1(2) of the Tax Procedure Code as correct determination of taxes and ensuring their payment. The application of the basic objective of tax administration to the payment on breach of budgetary discipline depends on the nature of the payment, which by its scope significantly exceeds the extent of this article.

Pursuant to article 3 of Act No. 166/1993 Coll., On the Supreme Audit Office, as amended (hereinafter referred to as the "Supreme Audit Office Act"), Supreme Audit Office is another state authority authorized to audit public financial subsidy from the state budget and the budget of the European Union. In these cases, the Supreme Audit Office also audits municipalities

and regions. However, control activity is limited to the conditions of public financial subsidy. The object is the same as in the case of public administration control or tax audit. The Supreme Audit Office's audit procedure is regulated in articles 19 et seq. of the Supreme Audit Office Act.

3 The proposed extension of the Supreme Audit Office's competences

At the end of 2018, a government bill was submitted to the Chamber of Deputies of the Czech Republic to extend the competence of the Supreme Audit Office to territorial self-governing units. From the legislative-technical point of view, these are two proposals – one amending the Constitution of the Czech Republic and the other amending the Supreme Audit Office Act. The substance of the proposal is to extend the Supreme Audit Office's competences to audit of regions and municipalities with extended competences (municipalities that provide state administration in the widest extent) and to the audit of their established organizations and organizations in which they have ownership interests. Business companies established by territorial self-governing units and companies in whom municipalities and regions have an ownership interest are currently subject to state management and control only if they are applicants or recipients of public financial subsidy from the state or European budget. As stated above, the subject of this management and control is only the fulfillment of the conditions under which it was granted.

It is one of many attempts to extend the Supreme Audit Office's competences to municipalities and regions (the eighth bill submitted to the Chamber of Deputies of the Czech Republic). Older proposals did not limit audit to regions and municipalities with extended competences, but included all municipalities without exception. According to the explanatory memorandum of the Government's bill, the restriction was based on experience from the Slovak Republic. The Supreme Audit Office of the Slovak Republic audits the financial management of all municipalities without exception. According to the petitioner, however, the audit of smaller municipalities is less efficient. Furthermore, the petitioner bases his proposal also on the legislation of Austria, which allows the Supreme Audit Office to audit only

municipalities with a population of over 10 000. In the course of discussions on the bill in the previous parliamentary term, the population criterion was rejected by the Government's advisory body – the Legislative Council of the Government as a biased criterion that does not indicate the significance of risks to public funds. It can only be assumed that the main reason for a narrower extension of the Supreme Audit Office's mandate was the endeavor of the petitioner to successfully complete the legislative process. The introduction of further audit over the management and control of municipalities and regions is always accompanied by a fundamental negative attitude of a number of deputies and senators, regardless of their political affiliation. The main reasons that they give are the unconstitutionality and excessive control burden that already affects municipalities under the current legislation. However, the argument of unconstitutionality has already been refuted, even though it was in fact a decision to assess the constitutionality of the rules on budgetary liability. The Constitutional Court in its decision Pl. US 6/17 stated that ownership of territorial self-governing units (Article 11(3) of the Charter) obliges them to protect the interests of their citizens, because this is the reason why they have property. This also implies the obligation of local and regional authorities to dispose of their assets economically, responsibly and in accordance with the requirement of due care. The basic criterion used by the Constitutional Court to verify the constitutionality was the question whether the relevant legislation did not empty or eliminate the content of the constitutional right to territorial self-government. Of course, the Constitutional Court's decision cannot be anticipated in the case of an amendment to the Supreme Audit Office, but it cannot be assumed that the arguments would fundamentally change if the Supreme Audit Office's competences were extended. For the sake of completeness, it should also be pointed out that the amendment to the Supreme Audit Office Act is also linked to an amendment to the Constitution of the Czech Republic, i.e. it is a fact that the Constitutional Court would have to take into account.

4 Influence of the extension of the Supreme Audit Office's competences on protection of public funds

In order to verify the efficiency of the proposed extension of the Supreme Audit Office's competence to protect public funds, it is essential to compare the efficiency of the existing management and control system and the newly proposed audit. The audit of the Supreme Audit Office, as proposed, will not be more extensive than the financial management and control review of territorial self-governing units. The object should be the same. If the legislator had to choose between the review and the newly proposed audit of the Supreme Audit Office, it would necessarily have to conclude that the review has a much larger scope. It is periodic, annual review of all municipalities and regions, regardless of the activities they provide or their size. On the other hand, the Supreme Audit Office will carry out the audit on a selective basis, i.e. for the most risky entities and in the case of municipalities, it will be limited not only by the significance of the risks associated with the management and control, but also by the scope of the administrative activities they provide. The competences of the Supreme Audit Office, as it is proposed, will apply only to municipalities with extended competences.

For this verification it is not only the results of the audit activity that are decisive, but also the costs for it. Effective management of public funds means that the best possible relationship between the funds used and the results is achieved. That is, a control activity that focuses on the most significant risks, even if it is not across the board, can achieve a higher level of efficiency than audit that is across the board regardless of the significance of the risks. In essence, this means that if the selection of risky municipalities is set correctly, the audit of Supreme Audit Office may be more effective than the annual review of municipal management and control, even if it is not across the board. However, the proposed extension of the Supreme Audit Office's competences does not foresee the abolition of the financial management and control review of territorial self-governing units. De facto, there is only an additional audit element for regions and municipalities with extended competences, which will have the same scope and object as the already set system of annual review. With regard to the fact that there will

be an increase in the costs of carrying out control activities, but the scope and object matter will remain the same, it can be concluded that the hypothesis stated in the introduction is not confirmed. To increase efficiency of the protection of public funds is not enough to make a legislative change, even the legislative change is not sine qua non condition.

5 Conclusion

The financial management and control of territorial self-governing units in the Czech Republic is based on the basic setting of redistribution of public funds. Territorial self-governing units, i.e. municipalities and regions, manage and control public funds, even though they have the status of independent public corporations with their own property in terms of the Constitution of the Czech Republic. The primary source of local and regional authorities is public funds collected at national level. The financial management and control of municipalities and regions is a basic prerequisite for ensuring economic, efficient and effective spending of the funds entrusted to them. The analysis verified that the existing management and control system make it possible to manage and control the territorial self-governing units in their entirety. The hypothesis set in the introduction, that the proposed extension of the Supreme Audit Office's competences to territorial self-governing units in the Czech Republic will increase the efficiency of the protection of public funds, has not been confirmed. By extending the competence of the Supreme Audit Office, the scope of financial management and control will not be extended. The key to increasing the efficiency of the protection of public funds managed by local and regional authorities is not simply to supplement another audit institution, but to increase the efficiency of existing control activities, or to replace existing control activities with a more efficient control mechanism. Under certain conditions, it may also be an extension of the Supreme Audit Office's competences. However, it should be noted that the proposed amendment does not meet these attributes.

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Is Privatization of Public Tasks a Chance for Decentralized Actions of Local Government Units?

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Abstract

The aim of the considerations is to answer whether, and if so, to what extent, the applicable legal regulations allow the possibility of privatizing public tasks, in particular at the self-government level. The answer to this question is extremely important from the viewpoint of the activities of local government units, which, on the one hand, due to the decentralization of public power have been granted the rights to carry out a substantial part of public tasks. On the other hand, after granting them certain powers, they have an insufficient guarantee of access to financial resources, which, considering both the doctrine and practice, can be treated as a hypothesis of the study.

Considering the above, the legislator allows the possibility of another way of raising the necessary funds, which can be linked to the privatization of the so-called self-government public tasks mentioned in the title. Of course, due to the special nature of these tasks, privatization is subject to many statutory restrictions, which the study will discuss only in the selected scope.

The considerations contained in this article are based on the applicable legal regulations, doctrine, and judicial decisions; hence the basic research method to be applied in the study will be the dogmatic and legal method.

Keywords: Privatization; Public Tasks; Municipal Economy; Public Benefit Sphere; Non-Governmental Organizations (NGOs); Capital Companies.

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1 Introduction

As it results from the title, the study will be devoted to some considerations aiming at answering the question posed by the author. Being aware of the fact that the chosen issue is quite controversial, and the formulated question is perverse, the author's goal is to indicate the applicable legal regulations, which increasingly used in practice by local government units, make the implementation of the self-government public task dependent on transferring it to a private entity. This state of affairs is enforced by the lack, often proven in the doctrine, of sufficient, adequate financial resources, which can be treated as a hypothesis of the study.

This issue is extremely important because the implementation of public tasks in the privatized form undermines the essence of this kind of tasks. Indeed, these tasks being public, and not private, should be implemented by public entities designated by law, which is to guarantee their public nature. At the same time, their public nature can be seen from two points of view. Firstly, as entities of the public finance sector appointed by law to perform these tasks based on financial resources contained in the adopted annual budget, which is to ensure their proper (in accordance with the law) spending. Secondly, it is related to the indication of the importance of the public nature understood as the definition of the list of recipients, for whom these tasks are to be implemented – in the case of the self-government level, residents forming a local or regional community.

To approximate the title issue, only those legal regulations will be mentioned that allow, and sometimes even encourage self-government tasks to be transferred to private entities. Due to the technical requirements, the conducted considerations will be selective, and they will exemplify the analysed issues the most.

They will be based on applicable legal regulations, selected professional literature and judicial decisions. Mentioning them, as part of the dogmatic and legal method, will form the basis for formulating the answer to the question posed in the title of the article.

2 Decentralization of public authority and its impact on the financial feasibility of public tasks

The decentralization of public authority[2] in Poland guarantees the entitlement of self-government bodies to carry out these public tasks (objectives) (Jellinek, 1924: 101; Stahl, 2007: 95) that are not reserved for other bodies[3]. On the one hand, it is undoubtedly, a huge privilege for a self-government level; on the other, however, also a great financial burden. The doctrine has repeatedly pointed out that an important part of the tasks delegated to self-government units[4] (hereinafter also referred to as the local government units – l.g.u.) is disproportionate or even grossly disproportionate to the number of self-government public tasks (Stasikowski, 2009: 10); therefore, there appeared statements of inadequacy of tasks to funds allocated to l.g.u. (Feret, 2014: 53–70; Hałaburda, 2018: 92).

Local government units are to carry out public tasks[5], important not only for the residents living in the areas of individual self-government units (Augustyniak, 2017: 374–395), but also those constitutionally indicated and recognized as the most important from the point of view of the entire state, e.g.: in the field of education[6], health[7], or culture[8]. Due to the importance

2 It follows directly from Art. 15, section 1 of the Constitution of the Republic of Poland of 2 April 1997, Journal of Laws, no. 78, item. 483 as amended., hereinafter also called the Constitution of the RP.

3 Based on Art. 163 of the Constitution of the RP.

4 See Art. 16, section 2 of the Constitution of the RP.

5 The term "public tasks" indicates that they can be carried out by various entities that are not authority organs and without the need to transfer these tasks to them, and that they are characterized by universality and benefit to the public, as well as promoting the achievement of the objectives set out in the Constitution or the statute. For more information see the Supreme Administrative Court Judgement of 18 May 2006, I OSK 2415/15, and the Supreme Administrative Court Judgement of 18 August 2010, Ref. Act I OSK 851/10. Available at: https://orzeczenia.nsa.gov.pl

6 Quoted after Art. 70, section 1, sentence 1 of the Constitution of the RP, "Everyone shall have the right to education".

7 Quoted after Art. 68, section 1 of the Constitution of the RP, "Everyone shall have the right to have his health protected".

8 "*The freedom of artistic creation and scientific research as well as dissemination of the fruits thereof, the freedom to teach and to enjoy the products of culture, shall be ensured to everyone*".- Art. 73 of the Constitution of the RP.

of these tasks clarified in the so-called self-government laws[9], the legislator indicated a list of public entities named the public finance sector[10], responsible for their implementation on the basis of public funds specified in the budget. However, even in this case, the legislator consented, within the separate laws, to the implementation of public tasks in other forms than those provided for in said list[11].

In addition to those entities, it empowered others to use and dispose of public funds in the specified scope[12]. And it is this legal regulation and the aforementioned possibility of public tasks being carried out by entities from outside the public finance sector that should be treated as a basis for the privatization of public tasks mentioned in the title.

3 Characteristics of organizational and legal forms implementing local government public tasks

Considerations in this respect should be started from the principle of public tasks implementation also at the local government level, according to which the public finance sector bears the burden of public tasks implementation based on the public funds allocated annually. Referring this principle to the local government sector of public finance (Miemiec, Sawicka, Miemiec, 2013: 311)[13], it should be noted that it is the local government units and their federations and metropolitan federations that are to carry out public tasks indicated by the provisions of the local government laws. These tasks

9 The Act of 8 March 1990 on the Communal Government is mentioned here, the consolidated text, Journal of Laws of 2018, item. 994, as amended; the Act of 5 June 1998 on the District Government, the consolidated text, Journal of Laws of 2018, item. 995, as amended, and the Act of 5 June 1998 on the Provincial Government, the consolidated text. Journal of Laws of 2018, item 913 as amended.

10 It is based on Art. 9 of the Act of 27 August 2009 on Public Finances, the consolidated text. Journal of Laws of 2017, item 2077 as amended).

11 Quoted after Art. 8 of the Act on Public Finances.

12 Under Art. 4, para. 1, point 2 of the above Act.

13 On the basis of the applicable regulations of the Act on Public Finances, there is no such legal concept, although the professional literature often uses it, which can be considered as a certain "legacy of the past" having its roots in the first Act of 26 November 1998 on Public Finances (the consolidated text Journal of Laws of 2003, no. 15, item. 148 as amended), which divided the public finance sector into central government and local government sectors.

are carried out in the form of budgetary units[14], operating fully on the basis of public funds specified in the budget resolution.

However, even in the case of the public finance sector, the aforementioned possibility of implementing public tasks through organizational and legal forms legally specified directly in Art. 9, points 3–7, and point 14 of the Act on Public Finances, or through forms resulting from the provisions of separate statutes.

The task of health care should be referred to as the first example in this regard. This task, to which the Constitution of the RP assigns a great importance, in principle, is to be implemented in the form of a budget unit[15], or an independent public health care institution[16], whose activity will be subject to the characteristics while analysing the provisions of a separate Act on Medical Activity[17]. It turns out that the legislator placed an entrepreneur in the first place[18]. This entrepreneur operating in the form of a capital company: a limited liability company or a joint stock company[19], is to provide health services as part of the public task, which undoubtedly confirms the partial privatization of the health care task in the case of the commune *(gmina)* (Bandarzewski, 2007: 339), and the protection and promotion of health in the case of districts *(powiat)* and provinces *(województwo)*[20]. This is also confirmed by the regulations of the Act on Municipal Economy[21], assuming that local government units may entrust by contract

14 Although in the case of tasks in the field of education, the legislator introduces a caveat consisting in separating a bank account. For more on this subject see Art. 223 of the Act on Public Finances.

15 Referring to the form of financing the public task implementation, the legislator distinguished and still relies on the distinction between two ways of budgeting (financing) units of the public finance sector, which can be equated, following the doctrine, with those related to the budget economy and extra-budgetary economy. The first case refers to the activities of entities financially completely related to the budget, which should be treated as a rule.

16 Quoted after Art. 9, point 10 of the Act on Public Finances.

17 The Act of 15 April 2011 on Medical Activity, the consolidated text, Journal of Laws of 2018, item 160 as amended.

18 Under Art. 4, section 1, point 1 of the Act on Medical Activity.

19 See Art. 69 of the above Act in conjunction with the Act of 6 March 2018 – Law of Entrepreneurs, Journal of Laws, item 646, as amended.

20 According to Art. 4, section 1, point 2 of the Act on the District Government and Art. 14, section 1, point 2 of the Act on the Provincial Government, respectively.

21 Quoted after Art. 3, section 1 of the Act of 20 December 1995 on Municipal Economy, the consolidated text of 2017 item 827 as amended.

the implementation of tasks in the field of municipal economy to natural persons, legal persons, or organizational units without legal personality.

The situation is similar when talking about independent public health care facilities. In this case, it seems that the legislator clearly encouraged the performance of tasks in the form of companies, as evidenced by the content of Article 190 of said Act. According to its wording: "*If the creating entity transformed an independent public healthcare facility into a capital company (…) in the period until 31 December 2013, liabilities of the creating entity taken over from the independent public healthcare facility (…) shall be discontinued*".

The same applies to another public task, defined constitutionally and regarding education. In addition to the abovementioned caveat, in the form of the possibility to separate a bank account, the legislator in the Act on Educational Law[22] creates, apart from the principle of running schools and facilities by public administration bodies[23], the possibility of supporting this activity by non-governmental organizations, including scouting organizations, as well as legal persons running statutory activities in the field of education and upbringing[24]. These entities, not included in the public finance sector and not acting in order to make a profit, may receive from the budget of a local government unit targeted subsidies for public purposes related to the implementation of this unit tasks, as well as co-financing of investments related to these tasks[25]. In this case, the local government unit enters into a contract with a unit that will carry out the task.

The situation is different in the case of tasks in the field of culture, where at the local government level, as a principle, they are to be implemented by local government institutions of culture[26], because it is a local government own task of a mandatory nature. However, the legislator allows for the possibility of organizing and conducting cultural activities also by legal persons, natural persons, and organizational units without legal personality[27]

22 The Act of 16 December 2016 on Educational Law, the consolidated text, Journal of Laws of 2018, item 996 as amended.
23 Quoted after Art. 3, section 2 of Educational Law.
24 According to Article 3, section 1 of Educational Law.
25 Quoted after Art. 221 of the Act on Public Finances.
26 In accordance with Art. 9, section 1, and section 2 of the Act of 21 October 1991, the consolidated text, Journal of Laws of 2018, item 1893.
27 In accordance with Art. 3, section 1, and section 2 of the above Act.

unless they are not business activities. In this case, due to the patronage of the State over this kind of tasks, the entity conducting cultural activities may also receive grants from the State budget[28].

4 Local government public tasks carried out in the sphere of public benefit

Returning to the privatization of public tasks mentioned in the title (Katner, 2003: 26; Strzyczkowski 2005: 155–158), one should refer one's considerations to the possibility of creating organizational units operating both in the sphere of public benefit and beyond it. In these aspects of local government activity, one should seek the possibility of full privatization of tasks. In order to study this aspect of functioning of l.g.u., it is necessary to refer to two groups of legal regulations: constitutional and resulting from ordinary statutes, closely related, and mutually permeating. These concern regulations related to the abovementioned Local Government Acts, the Act on Municipal Economy, and the Act on Public Finances.

As a rule, it should be presumed that the local government units, as well as their federations, act to perform public tasks. These public tasks, sometimes also referred to as public objectives[29], are characterized by their public benefit consisting in the satisfaction of collective needs of the local community. In keeping with the statutory regulations, it can be assumed that the l.g.u. act conducting municipal economy, which includes in particular public benefit tasks aimed at current and continued satisfaction of the collective needs of the population through the provision of widely available services. In order for municipal economy to be properly run, local government units may, in accordance with the provisions of the Local Government Acts, create organizational units, conclude contracts with other entities, even NGOs[30], and in the case of communes also auxiliary units[31]. In order

28 Quoted after Art. 5 of the above Act.
29 See Art. 221 of the above quoted Act on Public Finances.
30 According to Art. 9, section 1 of the Act on the Communal Government; Art. 4, section 22 of the Act on the District Government; Art. 12, section 1, point 4 of the Act on the Provincial Government, respectively.
31 See Art. 5 of the Act on the Communal Government.

to conduct municipal economy, they can create in particular commercial companies[32].

In order to specify other forms within which l.g.u. may act, it should be emphasized that it is very important for the legislator to delimit public tasks of the public benefit nature from those that go beyond this benefit. In this respect, the grounds are the regulations of the Local Government Acts, which allow communes[33] and provinces[34] to operate also outside the sphere of public benefit as opposed to districts that have not acquired such rights[35]. This is also important from the point of view of the Act on Municipal Economy, which also clearly indicates that only public benefit tasks can be implemented in the form of local government budgetary establishments[36] and others in the form, for example, of commercial companies as already mentioned above.

5 Local government public tasks that go beyond the sphere of public benefit

The key question emerging from the presented legal regulations is an indication when the legislator allows privatization of public tasks (tasks going beyond the sphere of public benefit). In order to answer the question formulated in this way, it is necessary to refer again to the abovementioned legal regulations, on the basis of which, although not directly, one can accept a certain presumption ordering these issues.

Starting the analysis from the basic local government unit, it is obvious on the basis of applicable legal regulations that, apart from the sphere of public benefit, the commune may create commercial companies and join them if the following two conditions are met concurrently: 1) there are unmet needs of the local government community on the local market; 2) there is unemployment in the commune which significantly affects the standard of living of the local government community, and the application of other

32 Quoted after Art. 2 of the Act on Municipal Economy.
33 Quoted after Art. 9 of the Act on the Communal Government.
34 Quoted after Art. 13, section 2 of the Act on the Provincial Government.
35 Quoted after Art. 6, section 2 of the Act on the District Government.
36 It follows from Art. 7 of the referred Act.

actions and legal measures resulting from the legislation in force has not led to economic activation, and in particular to significant local market recovery or permanent limitation of unemployment[37]. The adopted regulation in this respect, although referring in general to the exclusive jurisdiction of the communal council is provided for in Art. 18, section 2, point 9f of the Act on the Communal Government.

In the case of communes, one should also refer to the regulations related to the functioning of another type of companies created from the transformation of municipal enterprises (Jagoda, 2001: 5; Czarnow, 2009: 38)[38] in relation to which if the communal council until 30 June 1997 had not decided about their organizational and legal form or about their privatization, on 1 July 1997 they were transformed into a company wholly owned by the commune, by virtue of law. As the regulations of the Act on the Communal Government indicate, this is a kind of legal person other than the commune, which can also carry out tasks that go beyond the sphere of public benefit[39].

When referring to provinces and the possibility of implementing tasks there, both in the sphere of public benefit and outside it, it is necessary to refer to the regulation which directly results in the possibility of creating capital companies[40]. An additional tightening of their activities is the performance of promotional, educational, publishing activities as well as telecommunications activities serving the development of the province[41].

As mentioned earlier, unlike communes and provinces, the districts have not been provided the opportunity to act outside the sphere of public benefit. However, due to the regulations under Art. 12, section 8g of the Act on the District Government, the legislator allows the district council to create them at the supra-communal level. In the sphere of public benefit, therefore, capital companies may be created as legal persons other than district ones to implement their own tasks.

37 It follows from Art. 10, section 1 of the Act on Municipal Economy.
38 Quoted after Art. 14, section 1 of the Act on Municipal Economy.
39 Based on Art. 43.
40 Art. 13 in conjunction with Art. 18, point 19e of the Act on the Provincial Government.
41 Art. 13, section 2 of the above Act.

6 Ways of implementing local public tasks by non-profit organizations

As mentioned at the beginning of the analysis, in the context of the privatization of local government public tasks, one should refer to the so-called other recipients of the provisions of the Act on Public Finances. This refers to the entities that may receive public funds to use or dispose of them in a certain range.

In the case of the budget of l.g.u., there is a possibility of granting such funds for units not belonging to the public finance sector and not performing tasks for profit, pursuant to the Act on Public Benefit and Volunteer Work[42], which uses the term of non-governmental organizations (also called non-profit organizations).

This concept was defined on the basis of Art. 3, section 3 of the abovementioned Act. On the basis of the adopted legal solutions, non-governmental organizations can be divided into two groups. The first group includes those that satisfy two cumulative conditions: 1) they are not included in the public finance sector, as defined in the Act on Public Finances, and 2) they do not work for profit-legal persons or entities without legal personality, the legal capacity of which is recognized by a separate statute, including foundations and associations (except political parties, trade unions and employers' organizations, professional self-governments, foundations established by political parties).

Within the second group, however, public benefit activities may also be carried out by: 1) legal persons and organizational units acting on the basis of the regulations on the relationship between the State and the Catholic Church in the Republic of Poland, on the relationship between the State and other churches and religious associations and on the guarantees of the freedom of conscience and religion, if their statutory objectives include conducting public benefit activities; 2) federations of the local government units; 3) social cooperatives; 4) joint-stock companies and limited liability companies and sports clubs which are companies operating under the provisions of the Act of 25 June 2010 on Sports[43], which do not operate for profit

42 The Act of 24 April 2003, the consolidated text. Journal of Laws of 2018, item 450 as amended.

43 The consolidated text. Journal of Laws of 2017, item 1463 as amended.

and spend all their income on the implementation of their statutory objectives and do not allocate profit to be distributed among their members, shareholders and employees (Sowiński, 2002: 119 et al.)[44].

The Act specifies enumeratively, although openly, the scope of public tasks belonging to the sphere of public benefit. Its regulations should be understood that these are the tasks that can be classified in the following ten groups: 1) social assistance, including assistance to families and individuals facing difficult situations, ensuring equal opportunities for these families and individuals, family support and foster care system; 2) charitable activities; 3) sustaining national tradition, cultivating Polishness, and the development of national, civil and cultural awareness; 4) activities for the benefit of national minorities; 5) health protection and promotion; 6) activities for persons with disabilities; 7) promotion of employment and professional activation of the unemployed and those threatened with dismissal; 8) protection and promotion of women's rights and the activities in favour of equal rights for women and men; 9) activities that support economic development, including entrepreneurship development; 10) activities supporting the development of local communities and collectivities[45].

As mentioned above, the specified list of public tasks is not exhaustive, due to the fact that the Act on Public Benefit and Volunteer Work also provides the possibility for residents of local government units, directly or through NGOs within the local initiative, to place a request for implementing a public task to a local government unit in which they are residents or have their seat. In particular, this initiative may include: construction, expansion or renovation of roads, sewage systems, water supply systems, buildings and architectural objects owned by local government units; schooling, education and upbringing; activity in the sphere of physical culture and tourism; nature conservation, including greenery in towns and villages; public order and security[46].

44 It follows from Art. 3, section 2, and section 3 of the Act on Public Benefit and Volunteer Work.

45 Based on Art. 4, section 1 of the Act on Public Benefit and Volunteer Work.

46 A detailed list of public tasks carried out at the request of residents is included in the text of Art. 19b, section 1 of the Act on Public Benefit and Volunteer Work.

It is important that non-governmental organizations acting in such a way can obtain a status of a public benefit organization provided that the activity defined by the Act has been carried out for at least two years. Additionally, non-governmental organizations and joint stock companies and limited liability companies and sports clubs are subject to entry in the National Court Register, along with which they acquire the status of public benefit organizations[47], or are designed to perform tasks, of course, within the scope of public benefit[48].

As a rule, this activity[49] may be conducted as an unpaid activity or as a paid activity (Art. 7–8 of the Act on Public Benefit and Volunteer Work). Unpaid activity takes place when there is no remuneration; *a contrario* it is payable when there is a remuneration and when it concerns the sale of goods or services produced or provided by persons directly benefiting from public benefit activities, in particular in the field of rehabilitation and adaptation to professional work of disabled people and professional and social reintegration of persons at risk of social exclusion[50].

It follows from the above that non-governmental organizations may conduct three types of public benefit activities: unpaid, paid or business activity. They should have a connection with the implementation of public tasks by the public administration bodies of both the central government and the local government. In this regard, the legislator in Art. 11 of the Act on Public Benefit and Volunteer Work provides for the possibility of commissioning

47 The entries are made according to the rules and procedures set forth in the Act of 20 August 1997 on the National Court Register, the consolidated text. Journal of Laws of 2018, item 986 as amended.

48 Detailed terms and conditions arise from Art. 20, section 1 of the above-mentioned Act.

49 In accordance with Art. 9, section 1 of the Act, the exception is paid activity of public benefit of non-governmental organizations and the mentioned above entities if it is an economic activity within the meaning of the provisions of the cited above Act on Law of Entrepreneurs if: 1) remuneration, in relation to the activity of a given type, is higher than that resulting from the costs of that activity, or 2) the average monthly remuneration of a natural person for employment in the performance of statutory public benefit activity for the last financial year, and in the case of employment lasting less than a financial year – for the period of this employment, exceeds three times the average monthly remuneration in the enterprise sector announced by the President of the Central Statistical Office for the previous year.

50 In the wording set out in Art. 1, point 1 of the Act of 19 August 2011 Amending the Act on Public Benefit and Volunteer Work and Some Other Acts, Journal of Laws, no. 209, item 1244, which came into force on 3 November 2011.

and entrusting performance of public tasks to these organizations. While in the case of commissioning performance of public tasks, the role of public administration bodies is to provide support, especially financial support, this entrustment means transferring specific public tasks to be implemented.

Both support and entrustment for the implementation of public tasks[51] take place after an open competition of offers unless separate provisions provide for a different ordering procedure. With the omission of carrying out an open competition, only extremely important tasks may be commissioned; they are connected with e.g.: natural disasters or technical failures in the country or abroad; the protection of human life or health, or because of an important social interest or important public interest, and in cases involving tasks in the field of civil protection and rescue[52].

In addition, it should not be forgotten that non-governmental organizations may, on their own initiative, submit requests regarding their willingness to perform a public task, including one that has been carried out in a different way to date, including by public administration bodies. However, such a request must meet certain statutory formal requirements, including, in particular, a description of the public task to be implemented and an estimate of the implementation cost of the public task. The submitted request initiates the procedure related to its evaluation, which is concluded with the possible signing of an agreement to support the performance of the public task or to entrust the performance of the public task.

The legal basis for launching financial resources for the implementation of public tasks by non-governmental organizations are legal provisions resulting from the regulations of the Act on Public Finances. The applicable regulations of the Act on Public Finances give this concept a particular rank. The fact that the notion of non-governmental organizations was already included in the initial provisions of the Act, in the glossary of terms used by its provisions, speaks in favour of its exceptional treatment. The legislator,

51 It usually occurs on the principles and procedures of the Act of 19 December 2008 on the Public and Private Partnership, the consolidated text. Journal of Laws of 2017 item 1834, as amended, or on the basis of international agreements, if the implementation of a particular public task involves transmitting non-refundable funds from foreign sources.

52 Quoted after Art. 11, section 2 of the Act on Public Benefit and Volunteer Work.

using the existing definition, defines NGOs as non-governmental organizations and entities mentioned in Art. 3, section 3 of the Act on Public Benefit and Volunteer Work (Szustek, 2008: 82)[53].

At the end of the analysis of legal solutions that demonstrate the possibility of privatizing local government public tasks, the extension of the list of entities responsible for the violation of public finance discipline also to private entities should be mentioned. According to Art. 4, section 1, point 4 of the Act, apart from entities associated with the public finance sector, such responsibility was also provided for persons executing on behalf of an entity not included in the public finance sector, which had been assigned for the use or disposal of public funds, some activities related to the use or disposal of such public funds. Such responsibility was also provided for in public orders, in relation to persons obliged or authorized to act on behalf of a public or private entity that offers auxiliary purchasing activities on the market, entrusted by the ordering manager to prepare, or conduct public procurement proceedings.

7 Final comments

How mentioned Janovec (2017), any legal entity, including the local government units have the chance to choice different ways on the financial market and get more possible sources of own financing.

As it is evident from the discussion on the possibility of the statutory privatization of local government public tasks, it should be noted that the applicable legal regulations form the basis for such an action at the local government level. Such authorisation is recognized during the analysis of units forming the public finance sector, within which the legislator points directly to other entities that will be able to carry out such tasks not only on the basis of public funds but also private funds.

In the light of the applicable legal regulations the recipients of the provisions related to the execution of public tasks may be divided into three groups: 1) public finance sector entities; 2) entities performing public tasks

53 It must therefore be assumed that the operation of non-governmental organizations in Poland is related to the activities of public benefit and volunteer work.

under the provisions of separate laws; 3) entities using or disposing of public funds under separate legal regulations. The operation of entities other than those covered by the public finance sector list is strictly contingent upon the provisions of law, which should be considered as conclusions *de lege lata*.

This restraint of the legislator, who heavily reserves the statutory implementation of public tasks is fully justified because it results from the public and not the private nature of these tasks falling within the sphere of public benefit. It is also important in this context that legal regulations more rarely provide for the possibility of the full privatization of public tasks (e.g.: in the field of culture), allowing more often incomplete privatization by co-financing the implementation of public tasks from the local government budget. This legislator's approach is completely understandable and worthy of approval. It should be regarded as exceptional and does not constitute a rule.

The issue related to the implementation of tasks going beyond the sphere of public benefit is a different matter, because, by their very nature, they should be admitted as types of tasks that can be privatized, thus relieving the budget from additional expenses. In this respect, however, it seems necessary to organize the provisions of law in such a way so that they should indicate in a transparent and condensed manner the premises and types of entities that can still carry out additional public tasks, which can be taken as requests *de lege ferenda*.

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Auction, as the Basis of Inefficient Expenditure of the Budget Resources in the Russian Federation

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Abstract

The topicality of the research is related to the analysis of the efficiency of the budget spending in the Russia, allocated by the customers for the State needs in the framework of the contracts concluded on the basis of e-auctions (auctions for the price reductions). The content of the research is aimed at a substantive assessment of the hypothesis of the inefficiency of the e-auction as a method of the selection of the supplier, performer to meet State needs at the expense of the budget funds. Objective is identification and substantiation of the facts (reasons), testifying to the ineffectiveness of the use of the budgetary funds in the framework of payment under contracts concluded on the basis of competitive procedures in the form of an e-auction. To show the importance of public financial interest in procurement and the lack of a fair balance of public and private financial interests due to the massive use of e-auctions. We have used comparative legal descriptions and interpretations; interviews with contract service customers; method of interpretation of the law; methods of formal and dialectical logic. It has been shown that excessive regulation of procurement and "forced legal imposition" of e-auctions on the Russian customers doesn't contribute to the achievement of real budget savings or the development of competition. In the United States, Europe and Asia, auctions are used in isolated and exceptional cases in the procurement.

Keywords: Public Financial Interests; Private Financial Interests; the Field of the Public Procurement; Customer; Procurement Participant; Transaction Costs; Budget Resources; E-Auction; Efficiency; Financial Expenses; Goods, Services; Public Procurement Law.

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1 Introduction

Currently, there is a tendency of a chaotic legal regulation of the field of the public procurement and complete disregard by the federal executive authorities of the private financial interests of the participants in procurement (business) and public interests of the customers, including public financial interests. From our point of view, this is due to the lack of a universal concept for the development and legal regulation of the public procurement in the Russia.

The Public Procurement Law (2013), which came into force on 1. 1. 2014, has undergone more than 54 changes. The number of the sub-legal regulatory acts, governing the sphere of the public procurement has exceeded 100 and continues to grow.

The federal executive authorities conceal the financial expenses of the key players of the public procurement (customers and procurement participants) related to the realization of competitive procedures, since the magnitude of such transaction costs is likely to exceed official statistics, reflecting the savings and efficiency in the use of the budget funds. Legal compulsion of customers to use e-auction as the main method of the determining of the counterparty doesn't contribute budget savings.

The Russia is in 57th place in the World Economic Forum efficiency rating of the World Economic Forum.

The practice shows that this hyperactivity of the legislative authorities, aimed mainly at the regulating of the competitive selection process of the contracting party under the contract, does not lead to an effective end result – timely reception of high-quality goods, works and services. The main method of the selecting a counterparty is a tender, with the exception of the list of goods, works, services that the government of the Russia ordered to acquire through the mandatory holding of an auction. This list is impressive in volume. Moreover, the new rules on the mandatory transfer of all competitive procedures from 1 January 2019 into an electronic form contain a rather complicated algorithm for the realization of the competition.

Therefore, it is more likely that we have the right to assert that the legislator has taken all the necessary measures so that the customer will choose the only "right" way – an e-auction in order to avoid problems and penalties.

The use of an e-auction (where there is one criterion – price) as the main and priority method for determining the counterparty is the main mistake of the legislator in the Russia. Many civilized countries have abandoned the priority application of the auction in public procurement. In addition, the more rapid transition to the electronic form of all purchases by customers in the Russia doesn't contribute to the efficient spending of the budget funds and the quality of the realization of the procurement procedures. For example, the EU directive 24/2014 provided for a smooth transition of customers of EU countries to purchases in electronic form from 1 January 2018. In the European Union, 48 months were spent on a thorough and comprehensive transition, rather than 6 months, as in the Russian Federation!

From our point of view, e-auctions cannot ensure equal accounting of public and private financial interests. The forced use of auctions has led to significant budget expenditures in the form of transaction costs. It should be noted that a single regulatory act in the Russia doesn't oblige you to consider these customers' expenses and take them into account when finalizing the efficiency of the public procurement. This is a serious mistake, leading to budget overruns and, accordingly, an imbalance of private and public financial interests in the field of procurement.

For example, perhaps, only lazy doesn't speak about the terrible condition and quality of the roads in Russia. But the construction and repair of the roads is carried out exclusively in the framework of public procurement and only through an e-auction!

The problem of mandatory use by the customers in the Russia of an e-auction as a priority method for determining a contractor in the field of the public procurement has allowed to formulate the main research hypotheses:

- the mandatory and mass application of auctions contradicts the experience and practice of the public procurement in many developed countries all over the world;
- the auction provokes the use of corruption and raider schemes. It leads to the delivery of low-quality goods, poor-quality work.

- the mandatory use of the auction, regardless of the price, leads to significant transaction costs for the customer;
- the result of the auction-one winner-one contract, leads to a quasi-monopolization of the market and higher prices for products or the result of works and services;
- the auction leads to a rise in the cost of goods, works, services at the expense of additional costs of commercial organizations for participation in the procurement: electronic signature, opening of special accounts in banks, the introduction of interim measures at each stage, obtaining of the necessary documents, etc.

The effectiveness of budget spending depends on:

- the value of the customer's costs on carrying out of the competitive selection;
- the costs of the commercial organization for the participation in the competitive procedure;
- the quality of the executed contractual obligation.

Consequently, it is advisable to conduct a competitive selection of the counterparty in the case when the effect of the saving on the auction exceeds the transaction costs of the customer. The process of such selection should be carried out by the ratio "price/quality" (public financial interests). Thus, it is possible to achieve real, not imaginary, savings in the process of conducting competitive procedures by completely abandoning the auction in the field of public procurement.

The consideration of the public financial interests of customers and private financial interests of commercial organizations (the cost of participation in the auction) is obligatory. The formation of a reasonable balance of these interests in the public procurement will contribute to providing customers with high-quality goods, works, services for their optimal cost, and developing the potential of private business, and at the same time reducing current transaction costs.

The transient transfer of the existing procurement model in full to an electronic form without adjustment and elimination of existing legal gaps and conflicts won't allow to save on the costs of the budget funds. On the contrary, such transition will require the planned costs of the realization

of the transfer of all procedures to the electronic form. After that, additional funds will be allocated to refine and eliminate errors and shortcomings that have not been eliminated earlier.

2 Materials and methods

The notion "interest" in the field of procurement hasn't been investigated currently, there are no scientific works and legal consolidation of the notion "interest" at the level of the law. Let's consider the content of the concept of financial interest through its types: public financial and private financial interests. The notion of "interest" is filled, first of all, with a philosophical source that predetermines the obligatory presence of the initial meaning and basis of goal-setting of conscious actions of certain social groups or each player individually. This is identical with the opinion of Hegel, who asserted that all actions of people are determined by their needs, passions and interests (Hegel,1993: 73).

Consequently, the activity of any player (subject) or group of players (players) aimed at achieving certain goals within the framework of a legal or non-legal field is dictated solely by the interests of such players (subjects). Iering, one of the first, considered the need of the subject in an individual or collective form in the notion of the "interest" (Iering, 1881: 30).

The State through the legal regulation of social relations, in fact, ensures the legality of the interests of some subjects (players) or a group of subjects (players) and prohibits other interests. We affirm that all public relations regulated by one or another rule of law are built, first of all, on the interest of each specific subject (player)or group of subjects (players) as a whole.

The notion "interest" in the field of the procurement can be briefly described as a specific behavior of any of the contracting party of the contract system based on a developed legal position to achieve its goals (needs). Therefore, in the sphere of the public procurement it is possible to distinguish the following parties (players, entities), whose interests don't only coincide, but also contradict each other:

- the interest of the customer – to receive goods, works, services of good quality with minimum budget costs in time;

- the interest of the commercial organization (counterparty)–to obtain the maximum profit within the framework of the contract and the fixed price of the contract offered to them or any other intangible benefit.

The interests of the customer are public interests, embodying the direct realization of the needs of an unlimited number of subjects (players) for the development of the society. The realization of such needs is formed not by the whole society, but by the State (authorized subjects (players), on legal grounds. At the same time, such a need cannot be limited by the State, since it is a guarantee of the development and functioning of the society as a whole.

The public financial interests of the customer may include:

- carrying out the procurement procedure taking into account the need for the criteria of "price-quality";
- timely and full receipt of goods, works and services of a proper quality;
- timely payment of the duly performed obligation under the contract;
- application of a penalty in case of violation of obligations under the contract by the counterparty;
- minimization of the costs associated with the choice of representation of interests related to administrative and arbitration disputes (minimization of transaction costs).

Among transaction costs in the field of the public procurement it is possible to distinguish the costs of: information costs, imperative costs of competition, measurement costs, costs of specification and protection of property rights, costs of opportunistic behavior (moral, corruption risks and tender raidership) (Kikavets, 2018: 1).

The interests of the counterparty are primarily private interests, which are determined by their bearers independently within the frames (limits) of the current legal regulation. As a rule, in most cases private interest develop into private financial interests of the supplier (contractor, performer).

The private financial interests of the counterparty may include:

- the minimization of the costs for the participation in competitive procedures;
- to provide market for products;

- the exclusion or minimization of the amount of mandatory security measures-transfer of funds to the customer's account or provision of a bank guarantee;
- the obtaining maximum profit, including through reducing costs in the course of fulfilling an obligation or transferring a part of an obligation to a subcontract (co-execution) for a lower cost;
- the minimization of the size of the penalty and other adverse moments in the case of customer complaints;
- the recovery of the funds from the State customer in case of an unreasonable refusal to pay the fulfilled obligation or late payment, including interest for the use of the improperly withheld funds.

The arguments presented above point to the diametrically opposed financial interests of the parties, the intersection of which in many cases may become a reason for a conflict. Do not forget that the conflict of financial interests is possible even without the participation of the public side (for example: the introduction of economic sanctions). However, even in such cases, conflicts of private financial interests indirectly turn into public financial interests with the need for State participation.

Commercial organizations" enter "into the public procurement voluntarily, without coercion, knowing about the "rules of the game": legal regulation, the importance and priority of State needs, strict sanctions for violation or non-fulfillment of obligations. The charters of commercial organizations contain a "sacred meaning"–an economic entity is created for profit. That is why commercial organizations won't take part in the transactions, in which not only the balance of responsibility of the parties is initially violated, but also there are increased risks. This is the reason for the low number of bidders in public procurement.

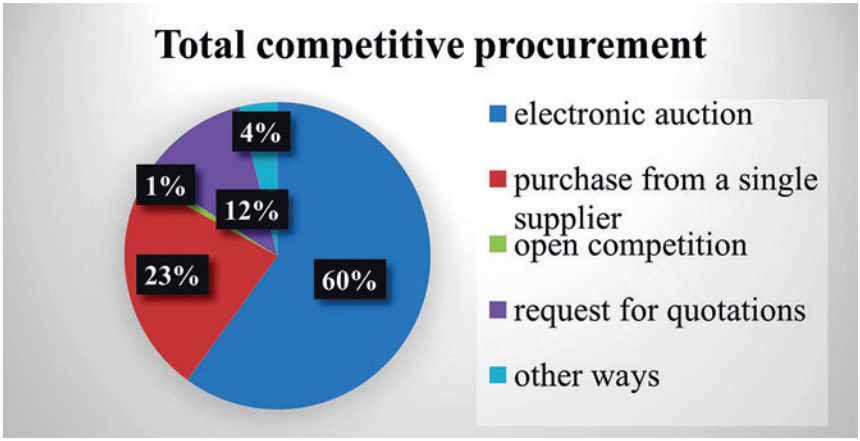
From our point of view, the contracts based on the results of competitive procedures are concluded by counterparties, which have either sufficient financial, material and labor resources, or customer loyalty, connected with, for example, with a long period of previously fulfilled obligations, business reputation, etc. In order to ensure equality (balance) of public and private financial interests, the Law on Public Procurement provides for the mandatory use of competitive procedures (mainly auctions) and model contracts.

The transfer of all government procurement to electronic form (to "figure") is the dream of the regulator (Ministry of Finance of Russia) and the controller of the procurement sphere (FAS Russia). According to their opinion, the electronic form will allow to minimize all costs of the parties, including the existing imbalance of interests. We are skeptical of this position. Everything that is happening now in the field of the procurement – the endless changes and chaos of rule-making is the result of a lack of goal-setting and a concept for the development of this area without real consideration of public and private financial interests. The use of e-auctions as the main method of determining the counterparty reduces the effectiveness of the use of the budgetary funds

If in the Russia in 2017 the share of e-auctions in procurement is 60 %.

The share of auctions in the total number of public procurement is shown in Graph (The Ministry of Finance of the Russian Federation. Statistical indicators characterizing the results of procurement for state and municipal needs in the I – III quarters of 2018).

Graph 1: Share of auctions in total government procurement



In fact, there has been taken place the substitution of the notions. World experience shows that the auction is massively used in the sale of existing goods (one auction organizer and several buyers). The legislation of the Russia provides for such an auction when selling the property of bankrupts

and privatizing State property. The situation in the field of the public procurement is completely different: the customer-buyer selects goods from several sellers (auction participants). The winner is determined only by the reduction of the price. The quality of the goods is only the promise of the seller, which the customer cannot verify until the conclusion of the contract.

It is appropriate to cite the research "On the Lemons Market" by J. Akerlof, which, despite numerous criticisms, clearly demonstrates the situation artificially shaped in the field of public procurement in Russia. It reflects the prevailing public procurement auction list, in which there is always only one winner, and according to only one criterion – the lowest price! (Akerlof, 1970: 8)

Trying to explain the difference in the pricing between new and used cars, J. Akerlof built a model of the "market of lemons" (Note author: "lemon"– so Americans call a used car in poor condition (the flaws are not visible from the beginning – they are hidden and are discovered only during the operation or by means of a comprehensive diagnostic expert).

Sellers of not quite high-quality used cars, using the buyer's ignorance or lack of competence through their unfair behavior (the buyer can't know about hidden defects) sell their car either at its market or at a lower price, thus crowding out bona fide buyers who can't sell their second-hand, but in good condition car below its fair cost. Consequently, the sellers of good cars prefer to drive themselves, rather than sell them cheaper cost. Conversely, buyers, preferring good cars will buy "lemons", as sellers of "lemons" are ready to "fall" in price.

Knowing the mechanism of the "lemon", the buyer can request all the documents for the car maintenance, for a small fee to diagnose by an independent expert, or buy a car from an intermediary with a good reputation. This will not fully help to filter out all the "lemons" on the market, but will create an opportunity to support the market for both good and bad cars.

In the Russia, the customer also wants to know everything about the product being purchased, including the reputation of the supplier, but the Law on the Contract System doesn't allow this. The right of the customer to obtain the necessary information is regarded as restricting of the competition. This

is nonsense, but in fact the Law on the Contractual System prescribes customers to purchase goods, the quality of which can be checked only by the results of their delivery. This leads to a significant loss of time, numerous legal disputes, an neffective use of the budget funds. At the same time, not only public financial interest suffers, but also public interest in general does – distrust of the officials, whose activity don't provide public needs (provision of free medicines, social security of the population, etc.).

One of the most striking examples of the negative role of the auction in the field of the public procurement is the statistics on the procurement of drugs by the Moscow City Oncology Hospital No. 62. The hospital purchased medicines through competitive negotiations mainly from manufacturers. The pricing table for a number of drugs (Drug pricing table) purchased simultaneously in 2016 through competitive negotiations (Hospital No. 62) and the e-auctions (Moscow Department of Health) testifies to the financial inefficiency of the auctions (Naplakova, Rodionova, Shamakina, 2018: 12).

Table 1: Drug pricing table

INN	Brand	Dosage	Average price per unit, rub		Contract value difference, %
			Hospital No 62	Health care department	
Docetaxel	Novotax	20 mg	2 168,0	66514,3	+ 67
Docetaxel	Novotax	80 mg	7 500,0	25 308,5	+ 70
paclitaxel	Taxacad	6 mg/ml 16,7 ml (100 mg)	1 200,00	5 790,6	+ 79
Gemcitabine	Gemcitare	1 000 mg	630,0	2778,4	+ 77
Gemcitabine	Gemcitare	200 mg	217,0	471,7	+ 54
Irinotecan	all	20 mg/ml 5 ml	1 218,0	4 744,6	+ 74

The contracts concluded at the end of such auctions (as a rule, with intermediaries, and not producers) require significant additional expenses from the budget. The head physician of the hospital, A. Makhson, has repeatedly stated that auctions don't contribute to real financial savings when purchasing medicines.

Despite the statistics presented in the comparative table, the Moscow authorities obliged Hospital No. 62 to purchase medicines through auctions according to the rules of the Public Procurement Law, and the head physician of the hospital was dismissed.

In the field of public procurement, there is an urgent need to take into account the transaction costs of the customer during the auction. This is fully consistent with the research of G. Stigler, who argued that a world with zero transaction costs turns out to be as strange as the physical world without friction force (Stigler, 1972: 1).

The massive use of auctions has led to a tremendous increase of the costs in the sphere of the public procurement in Russia. The need to describe all the properties of the product and to prepare documentation on the purchase in detail led to an increase in the staffing level of the customer. These are additional expenses from the budget for wages and the organization of jobs. At the same time, the quality of the goods or work performed under contracts does not depend on the additional expenses of budget funds.

The effectiveness of any commercial organization in the Russia is profit. Profit is an income minus expenses. Projecting this fact on the procurement sphere, we find that the effectiveness of this sphere is not at all the savings obtained by reducing the price at the auction! The effectiveness of the procurement sphere is the difference that must be obtained as a result of the revenues received (the result of using purchases + savings) and the costs incurred by the customer for the implementation of procurement procedures (mainly organizational and transaction costs). Despite the fact that the presence of transaction costs of the customer is predetermined by the current legislation on public procurement, no government agency in the Russia isn't authorized to count transaction costs.

The given examples with the repair of roads or the purchase of drugs showed that the auction provokes and actually pushes customers in the field of public procurement to purchase low-quality, expired goods, or to accept the result of poor-quality work. All this together forms a fertile environment for the use of corruption schemes and collusion of the customer and potential supplier.

3 Literature Review

In the process of the research, the works of many scientists have been reviewed. M. Linders, P. Johnson, A. Flynn, G. Firon in their study indicated that auctions could be used only in extreme cases where the buyer should have the most clear idea about the specification of the goods, its technology, logistics of supply, etc. The presence of enormous ethical risks in the form of fraudulent schemes, destroying the reputation and the relationship between suppliers and customers, involves significant time and financial costs for holding auctions. In order to save, it is advisable to use competitive negotiations (Linders, Johnson, Flynn, Firon, 2007: 139–140).

On the other hand, authors such as W. Vickrey, E. Maskin, J. Riley, W. Samuelson, suggest the possibility of using the auction either to raise the price or to reduce it, but taking into account additional parameters and conditions or as the final stage of the competitive procedure.

The presented author's positions have allowed to formulate a hypothesis of the given research and, comprehensively examine the auction procedure taking into account the Russian realities.

4 Results

The research has showed that many world powers have completely or more abandoned auctions in the field of the public procurement. It is enough to give an example of the fact that it was not possible to find any research on auctions in the field of public procurement on the website of the National Bureau of economic research – the largest database of scientific works on the economy.

Analysis of studies of the works of the foreign scientists has showed a slight use of the auctions in the field of the public procurement. In many cases, these are auctions for price increases for the right to conclude a contract – that is, an auction for the sale of goods of the second or third price, providing guarantees for the balance of public and private financial interests. The use of auctions is due to the fact that the buyer acquires a specific product knowing both the product and the potential seller, or has legal rights

to receive information from the participant in the reverse auction and all necessary evidence of financial stability, availability of material and human resources to fulfill the obligation under the contract.

Consequently, potential auction participants may offer their value for the right to conclude a contract at a fixed price, knowing the amount of the obligation and the contract fee established by the customer, in other words, to participate in the auction for a price increase for the right to conclude a contract on the previously known conditions for its execution and payment.

The proposed variant of a competitive procedure will contribute to countering corruption, since the budget will allocate funds exactly as much as is really necessary to meet public needs under the contract. Private finances offered by the auction winner for the right to conclude a contract are transferred directly to the budget. The customer receives the performance of obligations under the contract for the best price. Direct budget savings at auction are replaced by income from the sale of the right of a commercial organization to conclude a contract with the State.

According to the results of the research we conducted during the period of the study and the preparation of the research, the polls with employees of the contractual services of customers in several regions of the Russia produced a similar conclusion.

Virtually all of the customer employees interviewed by us noted the ineffectiveness of the e-auction as a procedure involving numerous significantly affect the quality of the purchase result), and for the counterparty (significant participation costs, lack of understanding legal regulations governing public procurement). Also, all respondents noted a significant number of intermediary participants and the presence of raider actions in the process of e-auctions by unscrupulous commercial organizations.

5 Discussions

You shouldn't discount that in the modern world the number of auctions is growing every day, but this type of bidding is used to increase the price more often by many auction participants – buyers with the only seller of goods. At the same time, the product for buyers is known and

individualized. When selling or buying a particular product, there are such types of auctions as: English direct auction for price increase, reverse Dutch auction for price reduction, closed auction of the first and second price (Vickrey Auction), both for increase and decrease.

The basis of the closed auctions of the first and second price is the strategy of fair determination and formation of the first price by the auction participants, which they secretly submit to the seller (auction organizer). The winner of the closed auction is the one whose price is recognized as the best (the lowest or the highest of all offered). At the closed auction of the second price the winner pays (receives) the price following after its price.

Proving his theorem of the closed auction of the second price, Vikri derived a formula according to which only bona fide participants were necessary for the implementation of the auction, since otherwise the winner was the one who offered a higher or lower price, without taking into account the quality, reputation and other characteristics. That is why in such an auction both the bidder and the seller receive the same expected winnings.

Thus, the dominant strategy of behavior of the participant of the closed auction of the second price is based on the honest strategy of each participant, which forms the proposal of a fair first price. Forming a fair and fair first price not only increases the chances of a participant in a closed auction to win – the realization of private financial interest, but also contributes to taking into account the financial interest of the seller. The understatement or overstatement of the first auction price from the true (fair) price of a product minimizes the chances of winning, if a competitor honestly offers a fair price for the product.

Thus, it cannot be considered either in theory or in practice as an effective expenditure of budgetary funds the payment of the contract concluded with the winner of the auction, who actually promised to deliver the necessary goods to the customer at the lowest price.

We believe it is advisable to revise the conceptual approach to the realization of the procurement, by avoiding reverse auctions – price reduction, since it provides ample opportunities for unscrupulous procurement participants

who actually "play with budget funds, promising to fulfill the obligation". This reduces the ultimate effectiveness of procurement.

Our study showed the feasibility of establishing the ability of a customer to purchase goods, works, services without competitive procedures at its discretion, since competition is not an end in itself of procurement. The customer will not be responsible if the price of such a purchase will be several times higher than similar goods, works, services, the obligations of which are fulfilled without penalty sanctions.

6 Conclusion

Public and private financial interests in the public procurement should receive an increased and substantive attention from the legislative and executive authorities, since it is the balance of such interests that can meet public needs for goods and services for their optimal cost, while developing the commercial sector (business) that in the end will contribute to the overall growth of the economic potential of the State. The realization, accounting and legal regulation of the public and private financial interests are possible in the process of conducting competitive purchases in the framework of the price-quality relationship, without an e-auction, the procedure of which provides for only one criterion – price.

We confirmed the hypothesis about the inefficiency of an e-auction, demonstrating the inefficient spending of budget funds, additional transaction costs and the imbalance of public and private financial interests. The main solution to the identified problem is a complete rejection of procurement auctions.

An alternative (soft) solution is possible – an auction to increase the price, the right to conclude a contract with the declared amount of the obligation and its price. In this case, the customer will receive from the sale of the right to conclude a contract, and the counterparty will receive a guaranteed return on the results of the fulfilled contract obligation.

At the same time, the auction will not play the key role of selection, and the customer will receive the quality set by him. The above will contribute to the balance of public and private financial interests.

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Problems of Formation of Municipal Finance in the Russian Federation

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Abstract

In this article the author analyses the Russian experience of formation of municipal finance. The study highlights some issues in the field of tax administration, which were only partially resolved in the course of municipal reform in the Russian Federation. Using the method of comparative legal analysis and monitoring, the existing approaches to municipal taxes and finance in the scientific literature and municipal practice are analysed.

Keywords: Tax Law; Municipal Finances; Municipal Taxes; Municipal Budget.

JEL classification: K34; H72.

1 Introduction

This article presents the results of the analysis of municipal budgets and national legislation of the Russian Federation in the field of local government and taxes and fees.

On the basis of methods of system comparative legal analysis and monitoring the research of normative regulation of activity of municipal authorities of the Russian Federation on formation of local budgets is carried out, the main sources of their formation are investigated.

In general, a positive assessment of changes in the tax sphere in the field of local self-government is given.

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2 Analysis of the situation in the Russian Federation

Russian experts note that the current tax reform in Russia is aimed at solving the following tasks:

- correction of deficiencies in the existing tax mechanisms underestimating the potential level of tax revenues;
- introduction of new methods of taxation corresponding to the modern development of social and economic relations;
- strengthening the balance between Treasury (fiscal) and burdensome (regulatory) tax functions reflecting public and private economic interests;
- reasonable differentiation on a permanent basis of tax revenues between budgets of all levels of the budget system in accordance with the volume of their expenditure tasks (Berezin M. Y., 2006: 640).

At the beginning of the reforms of local self-government (2003–2005), it was transitional for the introduction of Federal law no. 131 'On General principles of local self-government organization in the Russian Federation', which was subsequently extended until 2009). The government of the Russian Federation, analyzing the financial condition of the territorial budgets, in its assessments indicated that local budgets are overloaded with obligations imposed on them by Federal legislation without providing sources of funding ('unfunded Federal mandates'). More than 80 % of the tax revenues of these budgets are formed by deductions from Federal taxes. Own taxes cover less than 15 % of the expenditure needs of regional and local budgets; the list and tax base of regional and local taxes are obviously insufficient to finance regional and local expenditures, while the powers to regulate these taxes at the regional and local levels are very limited (Assembly of the legislation of the Russian Federation, no. 34/2001, Art. 3503).

In this regard, the predominant part of revenues in local budgets is formed at the expense of the budgets assigned to them on a permanent basis of tax revenues of other levels of the budget system, regulating tax revenues transferred to local budgets from higher budgets on a short-term basis, as well as at the expense of financial assistance directed to local budgets by budgets of higher levels of the budget system.

Currently, there are 21945 municipal formations on the territory of the Russian Federation[2].

Table 1: Number of municipalities by subjects of the Russian Federation (as on 1 January 2018)

Artificially of municipal formations									
	total	municipal districts	including by types						
			urban districts		Intra-city districts	Intra-city territories of cities of federal importance	settlements		
			total	including intracity division			total	including	
								urban	rural
1. 1. 2008	24 151	1 799	521	–	–	236	21 595	1 734	19 861
1. 1. 2009	24 161	1 810	507	–	–	236	21 608	1 745	19 863
1. 1. 2010	23 907	1 829	512	–	–	236	21 330	1 739	19 591
1. 1. 2011	23 304	1 824	515	–	–	236	20 729	1 733	18 996
1. 1. 2012	23 118	1 821	517	–	–	236	20 544	1 711	18 833
1. 1. 2013	23 001	1 817	518	–	–	257	20 409	1 687	18 722
1. 1. 2014	22 777	1 815	520	–	–	257	20 185	1 660	18 525
1. 1. 2015	22 923	1 823	535	–	–	267	20 298	1 644	18 654
1. 1. 2016	22 406	1 788	563	3	19	267	19 769	1 592	18 177
1. 1. 2017	22 327	1 784	567	3	19	267	19 690	1 589	18 101
1. 1. 2018	21 945	1 758	588	3	19	267	19 310	1 538	17 772

If we analyze the data given in the table above, a steady tendency to reduce the number of municipal formations can be seen.

Only two types of municipal formations – the urban district and the intra-city territory of cities of federal importance – increased the numerical indicators from 521 to 588 and from 236 to 267 units, respectively.

2 The latest official statistics is dated 1 January 2018.

The first reason for the quantitative changes in the composition of municipalities is related to the entry into Russia of new subjects of the Russian Federation on the basis of the Federal constitutional law dated 21 March 2014; no. 6–FCL 'On the admission to the Russian Federation of the Republic of Crimea and the formation of new constituent entities within the Russian Federation – the Republic of Crimea and the city of Federal importance of Sevastopol' (Assembly of legislation of the Russian Federation, no. 12/2014. Art. 1201) and the Agreement between the Russian Federation and the Republic of Crimea about acceptance in the Russian Federation of the Republic of Crimea and formation as a part of the Russian Federation of new subjects which was signed in the city of Moscow on 18 March 2014 and ratified by the Federal law of 21 March 2014. no. 36–FL 'On ratification of the Treaty between the Russian Federation and the Republic of Crimea on the admission of the Republic of Crimea to the Russian Federation and the formation of new subjects within the Russian Federation' (Assembly of legislation of the Russian Federation, no. 12/2014. Art. 1202).

On the basis of article 3 of the Law of the city of Sevastopol dated 2 June 2014 no. 17-LS 'On establishment of borders and the status of municipalities in the city of Sevastopol ('*Sevastopolskie izvestija' (Sevastopol news) from 4 June 2014 no. 44–48 (1669)*) the intra-city territories of the city of federal importance of Sevastopol are municipal districts (9) and the city of Inkerman.

The second reason for the territorial transformations in the sphere of local self-government in Russia is the process of upsizing of municipalities by joining the urban districts of adjoining urban and rural settlements.

A powerful impetus to the unification process was the adoption of the Federal law of 3 April 2017 no. 62-FL 'On amendments to the Federal law 'On General principles of the organization of local self-government in the Russian Federation', which changed the very concept of 'urban district', providing for the possibility of entering into its composition of several settlements united by a common territory that are not municipalities (previously the district was defined as an urban settlement).

While earlier, the territory of the subject of the Russian Federation was delimited between settlements, then, under the new law – between settlements and urban districts (paragraph 1 of part 1 of article 11).

The third reason for the reduction in the number of municipalities is the lack of economic potential of municipalities (labor resources, activity of economic entities, ensuring regular tax revenues, as a result of financial resources to address local issues).

3 Comparative characteristics of the share of tax revenues in municipal budgets

The Russian legal literature has repeatedly emphasized the economic dependence of local governments on the state. In particular, Ovchinnikov I. I. writes that local self-government will be independent only if its powers are provided with an appropriate resource base (Ovchinnikov, 2012: 295). The colleagues Kudzhiev Z. A., Savenko T. N., considering these types of municipalities as urban and rural settlements, ascertain the actual absence of own income (Kudziev, Savenko, Modern law, 2/2008: 98). The colleague Leksin I. V. believes that 'the budgets of settlements in most cases entirely depend on the territorially larger municipalities or the state'.

Reut A. V. and Soloveva N. A. emphasize: "*there is a crucial question of the search for additional financial source of the state and municipalities. If municipalities had sufficient competence in public finances in general, and in the field of the taxation, in particular, they would play a significant role in increasing incomes of local budgets. Thus, the question of competence of local authorities in the taxation is topical in Russia*" (Reut, Soloveva, 2018: 487).

Mironova S. notes that local governments in Russia are limited in terms of establishing separate elements taxation for local taxes. (Mironova, 2018: 185).

Problems of financial independence and balance of local budgets are also considered by foreign authors, for example, by my foreign colleague Ivana Pařízková (Pařízková, 2017: 179). Our foreign colleagues, in particular, Zalcewicz A., point to the need of ensuring an appropriate level of own income for local government units without the necessity of relying on external financing. She emphasizes: "Pursuing public tasks is a constitutional and statutory obligation of local government units. At the same time, the problem of proper regulation of the area of their financing is a very important

issue; as, with no appropriate resources designated for this purpose, it may turn out that pursuing public tasks will be impeded or even impossible. (Zalcewicz, 2017: 246).

Our foreign colleague Franczak Agnieszka, defining the independence of local governments, includes taxing independence in the authority of local governments to levy taxes and charges as defined in the laws (Franczak, 2018: 67).

Chernikova E. and Bartsits I. point to the need for analysis of the taxes and levies collection rate of local budgets. The qualitative and quantitative indicators of the local budgets revenues reveal clearly the state of the economy of the corresponding territory (Chernikova, Bartsits, 2018: 44).

To prove the above-mentioned statements, we give the following examples[3]:

- Decision of the Council of deputies of the Mozhaisk municipal district of the Moscow region of 28 December 2017 no. 905/61 'On the budget of the Mozhaisk municipal district for 2018 and the planning period of 2019 and 2020' (http://docs.cntd.ru/document/548105787).
  - The main characteristics of the budget of the Mozhaisk municipal district for 2018 were approved:
    - total budget revenues of the Mozhaisk municipal district in the amount of 2 810 026,8 thousand rubles, including the volume of inter-budget transfers received from other budgets of the budget system of the Russian Federation in the amount of 1 650 073,5 thousand rubles (58,7 %);
    - total expenditure budget of the Mozhaisk municipal district in the sum of 2 889 780,2 thousand rubles;
    - budget deficit of the Mozhaisk municipal district in the amount of 79 753,4 thousand rubles.
    - Revenues to the budget of the Mozhaisk municipal district in 2018 from tax and non-tax revenues amounted to 953,3 thousand rubles (0,03 %).
- Income of the urban district of Troitsk in 2018 amounted to 2,071 million rubles, of which the property tax of individuals (personal

3 The author applied the method of random sampling of municipalities, using different types of formations (municipal district, urban district, urban and rural settlement).

income tax – Federal tax) 753 million rubles (36,3 %), land tax 151,1 million rubles (7,29 %), other taxes 32,7 million rubles (1,5 %).

In this case, local taxes among the sources of income are no more than 8,7 %.

- In the municipal formation of the city of Naberezhnye Chelny of the Republic of Tatarstan in 2017, revenues amounted to 8 308 573,12 thousand rubles, of which revenues from tax revenues amounted to 3 315 220,05 thousand rubles (39,9 %),
  - at the same time, revenues from local taxes amounted to 196 464,7 thousand rubles (2,3 %) for the property tax of individuals.
  - land tax in the amount of 678 451 thousand rubles (8,16 %) (https://docviewer.yandex.ru/view/1413713).

  Thus, only 10,4 % of revenues from total revenues are local taxes.
- In the budget of the Bezverkhovsky rural settlement of the Khasansky municipal district of Primorsky Krai, revenues for 2018 amounted to 5 366,3 thousand rubles, of which tax and non-tax revenues are 2102 thousand rubles (39,1 %) (http://i.bezverhovskoe.ru/u/d9/71a28872b411e88eacd048dcd2f6db/).

  Among tax revenues, 76,1 % is land tax and 9,5 % is personal property tax. Thus, revenues from local taxes account for 84,6 % of income.

But such a radiant picture is formed not due to the high economic potential of rural settlements, but due to the fact that state powers are not transferred to the level of rural settlements, and, accordingly, the funds of inter-budgetary assistance from higher budgets are, first, and second, the amount of deductions from federal and regional taxes, different from those in municipalities and city districts.

The table below provides a comparative analysis of the amount of deductions to the budgets of various types of municipalities.

Table 2: Comparative analysis of the amount of deductions to the budgets of various types of municipalities

		Town settlements Part 2 of article 61 of the Budget Code of the Russian Federation	Municipal districts Article 61.1	Urban district Article 62.2
1	personal income tax	10 %		15 %
	charged on the territories of urban settlements		5 %	
	charged on the territories of rural settlements		13 %	
	charged on inter-settlement territories		15 %	
2	unified tax on imputed income for certain types of activities		100 %	100 %
3	unified agricultural tax	50 %		
	charged on the territories of urban settlements		50 %	
	charged on the territories of rural settlements		70 %	
	charged on inter-settlement territories		100 %	
4	tax levied in connection with the application of the patent system of taxation			100 %

4 Comparative analysis of indicators of revenues of local budgets

If we speak about the whole situation in the Russian Federation, there have been positive trends recently according to the monitoring of municipal budgets conducted by the Ministry of Finance of the Russian Federation.

Thus, according to the official reports of municipalities in 2016, the total amount of revenues received by local budgets is 3 645,1 billion rubles, which is higher than in 2015 by 4,2 % or 148 billion rubles.

Own budget revenues, which are the means of municipalities aimed at local issues, increased in 2016, as compared to the previous year, by 93,6 billion rubles or 4,1 % due to the growth of tax revenues (5,4 %) and the volume of inter-budget transfers (excluding subventions) from the budgets of other levels of the budget system (4,2 %), and amounted to 2 352,0 billion rubles.

Reporting on the execution of local budgets in 2017 established the total amount of revenues received by local budgets in the amount of 3 845,7 billion rubles, which is higher than in 2016 by 5,5 % or 200,6 billion rubles.

Own budget revenues, which are the means of municipalities to address local issues, increased in 2017 compared to the previous year by 152,8 billion rubles or 6,5 % due to the growth of tax revenues (6,6 %) and the volume of inter-budget transfers (excluding subventions) from the budgets of other levels of the budget system (8,9 %), and amounted to 2 504,8 billion rubles[4].

The distribution of own revenues by types of municipalities in 2017 is characterized by the following structure:

- in the budgets of urban districts (including budgets of urban districts with intracity division, intracity districts, intracity municipalities of Federal importance cities received 1 281,5 billion rubles (51,2 %);
- in the budgets of municipal districts – 859,3 billion rubles (34,3 %);
- in the budgets of urban settlements – 165,5 billion rubles (6,6 %);
- in the budgets of rural settlements – 198,5 billion rubles (7,9 %).

At the same time, in comparison with 2016, in the volume of own revenues of municipalities, the share of own revenues of urban districts increased by 0,3 %, urban settlements by 0,1 %, the share of municipal districts decreased by 0,3 %, rural settlements – by 0,2 percent.

The growth of own revenues of local budgets as a whole was due to an increase in own revenues of urban districts and municipal districts by 7,2 % and 5,7 %, respectively (or 84,5 and 46,7 billion rubles).

4 Https://www.minfin.ru/ru/perfomance/regions/monitoring_results/Monitoring_local/results

The increase in tax revenues by 7,3 % (or 44,2 billion rubles), subsidies by 14,1 % (or 37,6 billion rubles), subsidies by 6,8 % (or 6,3 billion rubles), as well as other inter-budget transfers by 18,8 % (or 10,1 billion rubles) had a significant impact on the growth of own revenues of urban districts.

The main reasons for the growth of own revenues of municipal districts are an increase in tax revenues by 5,2 % (or 15,9 billion rubles) and an increase in subsidies by 9,7 % (or 19,6 billion rubles), subsidies by 7,0 % (or 11,5 billion rubles).

The growth of own revenues in local budgets in comparison with 2016 occurred in 68 subjects of the Russian Federation, in 17 subjects of the Russian Federation there was a decrease.

The highest rates of growth of own revenues of local budgets are observed in the following subjects of the Russian Federation (table 3)

Table 3: Regions-leaders in growth rates of local budget revenues

Russian Federation subject	Own income (execution), billion rubles		The absolute gain, billion RUB	Growth rate 2016/2015, %
	2015	2016		
Republic of Crimea	16,4	22,9	6,5	139,6 %
Voronezh region	28,9	37,9	9,0	131,1 %
Saratov region	20,1	26,3	6,2	130,8 %
Kostroma region	8,5	10,6	2,1	124,7 %
The Republic Of Sakha (Yakutia)	59,5	73,8	14,3	124,0 %
Republic of Kalmykia	2,6	3,2	0,6	123,1 %
Tambov region	14,6	17,8	3,2	121,9 %
Amur region	21,8	26,5	4,7	121,6 %
Tula region	22,0	26,1	4,1	118,6 %
Kabardino-Balkar Republic	5,4	6,4	1,0	118,5 %
Pskov region	7,4	8,7	1,3	117,6 %
Penza region	13,9	16,2	2,3	116,5 %
Republic of Chechnya	6,8	7,9	1,1	116,2 %

Execution of local budgets in 2016 and 2017 in the context of types of municipalities is presented in table 4.

Table 4: Execution of local budgets

Types of municipal formations	Deficit / surplus, billion rubles	
	2016 год	2017 год
– budgets of urban districts *	-16,5	-30,6
– budgets of intracity municipal formations	0,2	0,4
– budgets of municipal districts	11,5	-5,4
– budgets of urban settlements	-3,2	-2,0
– budgets of rural settlements	-2,0	1,1

* including budgets of urban districts with intracity division and intracity districts

According to the subjects of the Russian Federation, in the total number of municipalities that approved local budgets in 2017, 54,1 % of budgets were executed with a deficit, 45,6 % – with a surplus, 0,3 % of budgets were balanced.

5 Conclusion

Describing the overall situation in the tax sphere in the field of local self-government, it should be noted that the progress in the growth rate of own revenues of municipal budgets in 2017 is observed not so much due to an increase in revenues from tax revenues (only 7,3 %), but at the expense of funds coming from higher-level budgets: 14,1 % subsidies, 6,8 % subsidies, 18,8 % other inter-budget transfers (a total of 39,7 %).

The problem of balance of local budgets, despite the measures taken to reform the financial system of municipalities, has not been solved so far, as showed by the results of monitoring. In 2017, in the whole of the Russian Federation, the local budgets were executed with a deficit. The volume of expenditures exceeded the volume of revenues of local budgets by 36,5 billion rubles with a planned deficit of 168,6 billion rubles (in 2016, local budget expenditures exceeded revenues by 10,0 billion rubles).

We believe that the measures taken by the regional authorities related to the consolidation of municipalities, as well as the development of amendments to Federal legislation providing for the creation of municipal districts will not solve this problem. It is necessary to change radically the system of inter-budgetary relations, which would allow municipalities of all types to accumulate financial potential sufficient to address local issues without reciprocating movements with budgets of higher levels, when most of the tax revenues go up and in small quantities return again to the municipal level.

I would like to conclude my article with the words of our foreign colleague Richard Bartes: "*There are many ways to regulate public finance management in local government but choosing a specific way of regulation will always be a predominantly political choice*". (Bartes, 2018. 36).

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Civic Budgeting in Polish Local Government Units

Małgorzata Kopowicz, Anna Patyk, Alicja Śrubkowska[1]

Abstract

The purpose of the article is to discuss the idea of civic budgeting and attempt the evaluation of its impact on the functioning of a local government unit. The presented study tries to provide an orderly scheme for participatory initiatives since they initially appeared in 2011 until they were regulated for the first time in systemic legislation in 2018.

Keywords: Civic Budget; Participatory Budgeting; Local Government Unit.

JEL Classification: H72.

1 Introduction

There many problems connected with self-administration. One of the most important problems is that the distinction between the state-administration and self-administration was not carried out in a strict manner and this improper distinction may lead to enhanced conflicts of interest (Radvan, Mrkývka and Schweigl, 2018).

The growth of civic society drives a change in the manner in which management processes in the public sector evolve. The trending shift from elective democracy to a democratic society, in which citizens are treated not just as voters but also joint decision-makers, sets certain guidelines to still developing societies. (Kołodziej-Hajdo, 2017: 160) One might say that participatory budget is the quintessence of civic initiative and has a certain effect on civic attitudes. Citizens able to influence their commune feel more connected to other inhabitants. They also feel increased responsibility for

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communal property and investments undertaken by the commune, because they actively participate in planning local expenditures.

The basic factor required to develop civic society that actively participates in public decision-making is the democratic form of state government. This applies primarily to devolving competences to lower levels of government, especially local government (Wójcicki, 2013: 160). Another factor driving the development of participatory budgets can be found in the feeling responsibile and willing to "run" one's own city.

As part of this study, issues related to the regulation of participatory budget issues in Polish local government acts will be presented. The issue will be addressed primarily from the perspective of the act on municipal self-government.

The introduction of a term defining the civic budget, rules for its creation and application will increase the attractiveness of civic budgets and the involvement of the public in matters of local governments.

2 Background

Civic budgeting is a consultative process, first used in 1989 in the Brazilian city of Porto Alegre by the social democratic Workers' Party. This initiative responded to the increasing influence of new social movements emerging in the 1970s in opposition to the military dictatorship. One of the key principles applied in Porto Alegre was the high level of involvement of citizens in carrying out the entire participatory process (Sorychta-Wojsczyk, 2015: 424). However, the beginnings were far from easy. In the first year after the idea was launched, less than 1000 people took part in the voting. In early 21st century, participatory budgets and the involvement of citizens in the affairs of their "little homelands" began to develop in Europe. After 2000, the idea took off rapidly in Spain, France, the UK, Germany and Poland, among others (Krzewińska, 2013: 20).

2.1 Participatory budgeting in Poland from 2011 to 2018

The first civic budget in Poland was proposed by activists from the Sopot Development Initiative. In 2011, Sopot was the first Polish city to include

in its budget projects chosen by citizens by universal voting. Far from being a one-time event, the involvement of citizens in the life of the city has been continuously developed and fine-tuned. Drafting the budget with the participation of citizens was present even before the resolution of the Sopot City Council of 6 May 2011 on introducing a civic budget (Supreme Audit Office report, 2018: 7). The city organized meetings with inhabitants that served as a platform to exchange experiences and submit comments on the budget planned for the next year.

Shortly after launching the Sopot initiative, its model was adopted by other communes, and the solution rapidly gained wide popularity. Within two years, social consultations related to task implementation were held in over 50 communes.

Until 2018, civic budgeting was not a term recognized in financial law. Implementation of tasks related to participatory budgeting was not based on any specific legal foundation. Instead, it was a method for citizens to jointly decide the appropriation of a specific pool of local government unit budget resources for purposes of their own selection.

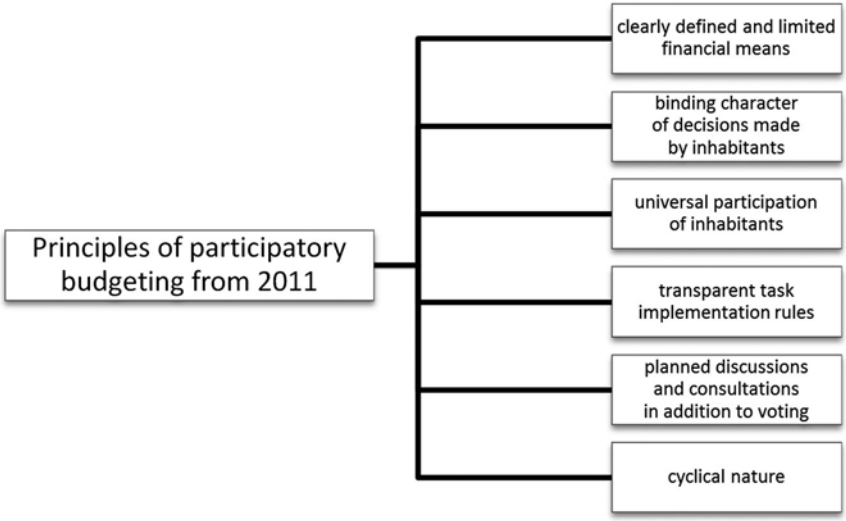
The legal foundation on which civic budgeting was originally based was Article 5a of the Commune Local Government Act that mentions social consultations held with commune inhabitants. One of the basic features of such consultations is their non-binding nature. Neither the consultations themselves nor their results created any obligation for local authorities. Both the first participatory budget and its subsequent editions during the next 7 years have been adopted under a peculiar contract between the citizens and authorities. An unwritten rule of social trust was observed in planning and implementing tasks related to the participatory budget. The implementation of these tasks should therefore not occur without the commune council adopting the relevant resolution as a legal foundation.

As a standard practice, consultations were and still are held in the period preceding the adoption of the budget for the new budget year. Expending the resources themselves also had to occur in line with effective regulations. The lack of detailed regulations in Polish legislation did not entitle local government units to spend resources on tasks related to participatory budget in an arbitrary manner – these resources had and still have to be spent according to the regulations in effect.

To find a place for civic budgets in Polish law from 2011 to 2018, the key issue was to clear doubts as to whether implementing such tasks was included in the commune's competences. Pursuant to Article 6(1) of the Commune Local Government Act, actions of the commune apply to all public matters of a local nature, unless reserved for the scope of activity of another entity under special regulations. It can therefore be assumed that public tasks are tasks involving benefits for the society, the entire population or the significant part of it, and taking into account public interest. In turn, in Article 7(1) of the Commune Local Government Act meeting the needs of the community is defined as performing tasks by the commune for the benefit of the entire population. According to judicial decisions, these provisions are task-related norms only and cannot be used to support authoritative acts of commune bodies.

In most communes the manner and method of staging social consultations are determined in a resolution of the commune council. The gathered experience shows that the participatory budget could have been defined using a number of rules that had to be strictly observed to ensure the proper and authentic participation of citizens in managing the commune (Szaranowicz-Kusz, 2014: 10).

Principles of participatory budgeting from 2011 to 2018



Source: own study based on: Szaranowicz-Kusz, 2014: 10

These rules did not form a definite list, but were rather a guideline for local government authorities on how to build long-term relationships with inhabitants. Defining strict time frames was immensely important. Once the tasks were chosen, a public ranking was drawn up and announced to the public. Each task was set for implementation with the new budget – in practice, the whole process ended before drafting the budget for the next year.

2.2 The situation following legislative amendments

In 2018, previous civic budgeting practices were put in order by subjecting them to legal regulations. The rules of drafting civic budgets in local government units were defined, and this was being done by setting the requirements for the contents of participatory budget resolutions adopted by commune councils, among others.

These provisions, which took effect in 2018, were the first to regulate and define civic budgeting. The Act on Amending Certain Acts to Increase the Participation of Citizens in the Process of Electing, Operating and Controlling Certain Public Bodies of 11 January 2018 (Article 1 of the Act on Amending Certain Acts to Increase the Participation of Citizens in the Process of Electing, Operating and Controlling Certain Public Bodies) amended the Commune Local Government Act, County Local Government Act and Province Local Government Act. In each of these acts, provisions stating that "*civic budgeting is a special form of social consultations*" (Article 5a of the Commune Local Government Act) were added.

Civic budgeting is alternately referred to as participatory budgeting, although the amended provisions undoubtedly use the former term. It is a decision-making process, open to opinions of inhabitants on how the local government unit budget should be drafted (Szlachetko, Bochetyn, 2014: 259).

Introducing the term "civic budgeting" in legal provisions regulating the functioning of local government in Poland is a novelty in itself. Until then, it was used customarily in a slightly provisional way. The new provisions began to apply to commune councils whose term started following the October 2018 local elections (Dorosz-Kruczyński, 2019: 1).

Since 2019, before adopting a new resolution on participatory budgeting, the commune council should apply the guidelines listed in the Act.

Article 5a(7) of the Commune Local Government Act defines the rules and requirements that must be met by a participatory budgeting project. They state as follows:

- Proposed projects must meet certain formal requirements which are necessary to correctly and properly examine the submitted applications. Each proposed project should undergo a formal and substantive appraisal.
- Each proposed project must be supported by the required number of inhabitant signatures. An additional requirement stipulates that the number of signatures may not be higher than 0,1 % of the total number of inhabitants of the territory covered by the participatory budget pool to which the project has been assigned. The council resolution must state the minimum number of inhabitant signatures which must be collected for a project to undergo an appraisal.
- Rules of appraising proposed projects as to their compliance with law, technical feasibility, meeting formal requirements and the manner of appealing against a decision refusing to submit the project for a vote should be adopted. Compliance with law is one of the most important requirements whose definition should not engender any doubts, not least because of the specific nature of tasks performed by local government units and legal limitations. The list of tasks that can be performed by local government units is considerably limited by statutory provisions. Technical feasibility should be understood as examining whether implementing the proposed task is feasible, whether the local government unit has at its disposal the required technical resources, and whether the proposal meets technology requirements. This rule is extremely important when planning tasks of an investment nature. The manner of appealing against the decision is a feature demonstrating the openness and transparency of public finances. Each filled appeal should be examined and any further decision concerning projects thoroughly justified.
- Rules of holding a vote, counting the results and notifying them to the public must be adopted. During each voting process, rules of conduct that ensure equal treatment of every voter must be employed.

> The direct voting principle is also of considerable importance. Equal treatment of voters means that each eligible person can cast only a single vote of importance on par with all other votes. There are no "more important" and "less important" votes. This principle of equality allows all voters to participate in the vote on equal terms. Each voter's vote carries equal weight and cannot be cast on behalf of someone else. Direct voting means that projects are chosen by a vote of citizens. There are no intermediaries and it is the inhabitants themselves who decide which tasks to select. After all, the vote is the crowning moment of the civic budget process. The choice of the voting method can considerably impact its credibility.

Article 5a(7) includes the words "in particular", which means that all requirements cited above are mandatory and must be considered. However, it doesn't limit the council's ability to adopt a resolution regulating other issues, subject to effective provisions of law.

The growing importance of participatory budgeting in Poland is evidenced by recent changes in the Commune Local Government Act (The Commune Local Government Act, Article 28aa(2)), County Local Government Act (The County Local Government Act, Article 30(2)) and Province Local Government Act (The Province Local Government Act, Article 34a(2)). These acts include provisions requiring that participatory budgeting be included in a local government unit's status report. The report includes a summary of the actions of executive bodies of communes, counties and provinces. Participatory budgeting is mentioned next to the implementation of policies, strategies and programmes and the resolutions of decision-making bodies.

2.3 The participatory budget as part of the commune budget

The changes concerning participatory instruments are especially applicable to cities with county status, which in Poland number sixty-six (http://eteryt.stat.gov.pl/eteryt/raporty/WebRaportZestawienie.asp [cit. 18 March 2019, 16:50]. The legislative amendments introduced impose on such cities the obligation to draft a civic budget. Article 5a(5) of the Commune Local Government Act mentions the minimum amount of planned resources set aside to implement civic budget tasks. These resources cannot account for

less than 0,5 % of commune expenditures shown in the previous budget implementation report. Since tasks related to participatory budgeting can be either property-related or current tasks, total expenditure must be taken into account when calculating the minimum amount.

A local government unit manages its finances based on a budget that is the annual plan of revenues and expenditures (receipts and payments). Pursuant to the wording of Article 5a(4) of the Commune Local Government Act, the tasks to be selected in participatory budgeting are included in the commune's budget resolution. They are therefore part of the budget, and their values should be mentioned in the budget resolution and listed in a separate schedule of expenditures. In budgets of cities with county status, there is a fixed minimum amount of expenditures which must be set aside for implementing participatory budgeting tasks, not less than 0,5 % of expenditures shown in the previous budget implementation report. In other local government units, the amount of such expenditures has not been defined. This means that the amounts of planned and implemented expenditures can be assigned arbitrarily.

It should be noted that both before and after the introduction of provisions regulating the definition and institution of participatory budgeting, the budget resources of a local government unit must be expended to implement specific tasks. Importantly, this must occur in accordance with separate regulations, such as Article 216(2) of the Public Finance Act. The provision lists in particular the following tasks:

- own tasks of local government units,
- public government tasks and other tasks entrusted to local government units by statute,
- tasks taken over by communes to be implemented under specific agreements or arrangements,
- tasks performed jointly with other local government units,
- material or financial assistance granted to other local government units,
- other programmes financed from public resources.

Especially notable is the provision of Article 5a(4) of the new 2018 Act, which states that tasks chosen in participatory budgeting cannot be removed

or significantly changed while the budget resolution is being drafted, a means of ensuring that the essence of tasks chosen by voting will not be interfered with. The provisions of the Act may, however, lead to numerous difficulties in performing the tasks. This can happen for example if interest in projects performed from designated resources decreases, if the tasks selected for implementation are not likely to fully satisfy the collective needs of all inhabitants, or if there are doubts as to their compliance with other tasks of the local government unit.

The newly introduced provisions concerning direct and equal voting also raise doubts concerning their application in practice. Granting the rights to vote without, for example, setting an age limit makes it possible to cast multiple votes in practice. The communes do not have the instruments necessary to sift out votes cast by minors through their legal guardians. Such voting also does not guarantee that the choice will be made directly. Thus, a prompt revision of provisions in this respect appears necessary.

2.4 Benefits and dangers

Introducing participatory budgeting brings benefits to inhabitants, non-government organizations, local government units and the private sector alike. Following Sorychta-Wojsczyk, at least four primary benefits resulting from the introduction of participatory budgeting in Polish local government units can be distinguished (Sorychta-Wojsczyk, 2015: 427–428).

Firstly, let's adress social effects. Taking part in the entire scope of work on participatory budgeting increases the role each inhabitant can play in making decisions for the collective. Citizens are more readily involved in social work and begin to perceive that contributing to the growth of their own community enhances the credibility of the commune and all its inhabitants. The process forgoes cohesion in the community.

The second noticeable group involves educational effects. During the process, knowledge on the workings of the budget, resource spending and functioning of local level authorities can be disseminated. With each passing year, more citizens become aware of how to draft a good project and where to turn for help and advice.

The third achievement involves economic effects. We can risk saying that even minor investments may contribute to improving the life of inhabitants in a community. Letting them decide what changes should be made enhances their quality of life.

The fourth effect includes increased trust in local government authorities. Like a good master of the house, a commune that promotes the idea of sharing its power and supports the efforts of citizens in joint decision-making is perceived as honest and trustworthy.

Based on experiences gained abroad and eight years of participatory budgets in Poland, we can also note the most important obstacles and difficulties faced by local government units when implementing participatory projects.

The first and undoubtedly one of the most important of these obstacles are financial resources. The need to involve additional money is caused not only directly due to the implementation of tasks, but also indirectly due to salaries of persons working to set up the system or promote the idea of the civic budget.

Another difficulty is ensuring that participation has a universal character. Local government authorities should set the objective of popularizing participatory budgeting among all commune inhabitants. No one should feel excluded and disregarded. The tools and resources used to popularize the contents must be suitable for the community in question.

The constant and rapid development of civic societies precipitates another obstacle that undoubtedly forms a huge challenge for local government authorities. The ever growing needs of involved inhabitants should be appropriately channelled. Reconciling the interests of inhabitants and local government authorities, having regard to the interests of the commune and limitations imposed by effective legal regulations, is a challenging and difficult undertaking.

3 Conclusions

Participatory budgeting has been a successful attempt to introduce a new method to manage public finances in Poland. The causes of increased interest in participatory budgeting have been noticed by M. Poniatowicz

(Poniatowicz, 2014: 182–183), among others. According to her, civic budgeting follows new trends and doctrines in public management. Participatory budgeting allows to stem the tide of a growing negative mood among voters and can also be used to decrease the level of frustration and increase interest in local government finances. M. Poniatowicz also stressed that civic budgeting limits the growing disparity between authorities and inhabitants, ultimately admitting that its use, popular and fashionable as it is, can serve as an instrument of territorial marketing.

It will not be an exaggeration to say that participation initiatives promote innovation and support the enterprise spirit among the inhabitants. They are also a forum where experience and feedback that is necessary for proper growth of both the society and its surroundings can be exchanged. To work out and develop an appropriate methodology for introducing and implementing participatory budgeting is undoubtedly a very difficult issue that requires a constant multi-dimensional dialogue. The benefits of civic participation and initiative cannot, however, be realized in full without setting up clear and understandable rules and principles.

As originally envisaged, participatory budgeting was to be a tool involving inhabitants in the process of spending public resources, bridging the gap between local government authorities and local communities. By inviting inhabitants to propose, vote on and control the correct implementation of tasks, introducing participatory budgeting may to a large extent influence the development and structure of civic society that becomes involved in local matters.

Making decisions and deviding tasks and proposals in participatory budgeting is meant to establish a common framework of cooperation and dialogue in the public space.

Statutory provisions for cities with county status, mandating that a minimum of 0,5 % of commune expenditures must be spent on tasks from participation initiatives, actually imposed on commune bodies an obligation to involve the inhabitants in local government affairs. With this, authorities were, to some extent, compelled to conduct more intense dialogue with inhabitants and encourage them to take an interest in developing their "little homelands".

One of the expected consequences of the passed amendment to regulations is mobilizing local government units to reinforce the initiatives undertaken by local communities. A change in regulations may trigger a long-lasting and complex reform of the management system in local government units. There can be no doubt that introducing legal regulations was necessary and satisfied a long-awaited need. Polish cities and communes, still in transition, need strong foundations to implement the participatory budget idea. Not all local government units are ready to use this tool. There can be no doubt, however, that they will have to adjust to changing conditions and legal provisions, as well as the increasing awareness of inhabitants.

The eight years of experience gained by the city of Sopot allow a realistic conclusion that this vision is far from improbable. After so many years, one can determine with high certainty the stages of drafting a participatory budget and its basic features. The fashionable trend of participatory budget took by surprise not only members of local government bodies, but also city activists and inhabitants. It is necessary to build on this trend and form a conscious and active society. Based on the experience of local governments and officials who undertook the responsibility to create and implement the first concept of civic budget, as well as its subsequent attempts in successive years, it can be said with certainty that working with a society that is becoming more involved is a big challenge for the authorities. Cooperation between local authorities, residents and associations should be further developed. It will enable the development of local governments and allow to build a conscious society. The regulations introduced in Polish law are valuable and necessary, but require fine-tuning and a deeper analysis of the participatory budgeting tool.

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An Attempt to Determine the Limits of Economic Activity of Local Government Units on the Local Market [1]

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Abstract

Undertaking and conducting commercial activity by local government units is an important matter both for the unit itself and for the local community expecting specific interventions on the local market. The role of local government units is not only to satisfy the needs of residents through the provision of services, but also the existence of these units as stimulators and organizers of local social and economic life. A local government unit should therefore take action for the benefit of this community, either through its own actions or indirectly, by activating other entities on the local market. However, it should refrain from this activity wherever it may threaten local economic operators or produce losses incommensurate to the benefits.

Keywords: Economic Activity; Public Interest; Local Government Units; Profit; Public Tasks.

JEL Classification: H71; H72; K2.

1 Introduction

Economic activity and public entity – these two notions invariably provoke questions about the possibility of conducting this activity, its scope and acceptable forms of running it by a public entity. The problem of admission of public entities to economic circulation should be considered in many

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areas, of which the legal level remains one of the most important, although not less important, from the point of view of the local community, seem to be those which concern the social and economic impact on the local market as a result of the public entity carrying out such activity. However, due to the problem indicated in the introduction, considerations will be carried out primarily on the basis of the normative layer, taking into account the practice of law enforcement.

As indicated in the introduction, the effects of admitting a public body to a sphere traditionally attributed to private parties must raise questions and concerns both in terms of public and private law. Undoubtedly a public entity, regardless of the way in which it chooses to carry out such an activity, is not a natural participant in economic transactions, and its involvement implies fears of possible losses inherent in the market play, or abuse of the dominant entity's position and thus distortion of fair and free competition. However, while agreeing with these arguments, it is important to recognise the danger arising from the schematic and disregarding changing conditions, limiting the role of local government units to the role of a passive observer of the economic situation on the local market. The retrospective interpretation of the provisions of the Acts regulating the admissibility of economic activity of local government units, or the analysis of judgments (often determining jurisprudence lines) concerning the boundaries of this activity, issued even before the recent economic crisis (which is discussed further in this paper), may be significant for further considerations. Despite the well described in the literature subject matter, the scope of conducting business activity by local government units, it still seems to be a grateful subject for conducted research and scientific considerations. However, in order to sort out preliminary issues, it is necessary to start with systemic regulations concerning the conduct of business activity by local government units.

2 Systemic regulations concerning economic activity of local government units

Systemic regulations concerning the position and functioning of local government in Poland directly concern the issues related to the admissibility and scope of conducting business activity by these entities. Due

to the political position, it is worth starting this part of the discussion with the commune, which is the basic unit of local government. In accordance with the provision of Article 9(1) of the Act on Municipal Self-Government, a commune and another municipal legal person may conduct business activity beyond the tasks of public utility only in the cases specified in a separate act. The same law contains a crucial definition of public utility tasks, which is important for further consideration. Public utility tasks, within the meaning of the Act, are the municipality's own tasks, as defined in Article 7(1), the aim of which is to meet the ongoing and uninterrupted satisfaction of the collective needs of the population through the provision of universally available services. Although the legislator has reserved the use of the notion of public utility to the Act on Municipal Self-Government, in other legal acts, it also uses this notion (e.g. the Act on Municipal Economy), which makes it universal in the entire legal system and allows it to be used also in relation to other local government units. In relation to other local government units, the legislator decided to diversify the legal possibilities of going beyond public utility tasks. In the case of counties, in the provision of Article 6(2) of the Act on county self-government indicated that the county may not conduct business activity going beyond the tasks of public utility. The legislator treated the activity of voivodeship self-government in a completely different way, indicating in the provision of Article 13 of the Act on Voivodeship self-government that apart from the sphere of public utility, a voivodeship may establish limited liability companies and joint-stock companies and join them if the activity of companies consists in performing promotional, educational, publishing and telecommunications activities subserving the development of the voivodeship. These solutions are confirmed by the provisions of the Act on Municipal Management, which in the provision of Article 10 indicates that the possibilities of conducting business outside the sphere of public utility are the domain only of communes and voivodeships with the exclusion of counties. Polish solutions are convergent with solutions used in many European countries. For example, under German law it is allowed to conduct business activity by local government units both within the limits of public utility and in certain conditions, beyond this sphere (Balcerek-Kosiarz, 2015: 308).

3 Public service limits

As indicated earlier, the main impulse for conducting the research in question was the difficulty in determining which type of activity falls within the scope of public utility and which types of activity of local government go beyond this sphere. The judgment of the Supreme Administrative Court of 16 May 2006 has become an important catalyst for these deliberations and at the same time the axis around which further deductions can be made. (II OSK 288/06, OwSS 2006/4/108), in which it was stated: The company's activity consisting in granting sureties for loans and credits contracted by local government units does not show any necessary elements to consider such activity as the performance of a public utility task. This type of activity cannot be regarded as a form of implementation of tasks aimed at the ongoing and uninterrupted satisfaction of the collective needs of the community. This verdict, despite the rather distant perspective of the issue, provokes questions both about the generic scope of conducting business activity by local government units, as well as the prerogatives for undertaking them. In order to answer these questions, it is first necessary to determine the scope of the definitions used by the legislator, concerning both the types of tasks performed by local government units, as well as to indicate the reasons for going beyond the scope of public utility. In the aforementioned provisions of Article 9 of the Act on Municipal Self-Government, the legislator generally allows to conduct business activity within the limits of public utility, and outside of it only in the cases indicated in the Act not specified in detail (it should be assumed that this is the Act on Municipal Management). The interpretation of these phrases leads to the conclusion that the notion of economic activity and public utility should be considered separately, since they can only overlap to a certain extent. As it is commonly stressed in literature and jurisprudence (see: Czerski, 2015, SIP LEX, *Judgment of the Supreme Administrative Court* (until 31. 12. 2003) in Gdańsk, of 9 January 2003. SA/Gd 1968/02), the fundamental difference between municipal management and economic activity is the fact that municipal management shall operate on a non profit making basis, but must fit within the framework of municipal activity, and its mandatory objective remains the performance of the municipality's own tasks, including meeting the collective needs

of the community (public utility tasks). The category of profit as an objective for economic activity should be an element which distinguishes normal commercial activities from those carried out within the framework of utilities. However, the occurrence of profit cannot be treated as an element excluding the recognition of the activity of a local government unit as the performance of municipal management. Profit is a secondary category from the point of view of the effect of public tasks and often depends on the type of task and the form in which the task is carried out.

Thus, the occurrence of profit is not a feature precluding the recognition of certain forms of activity of local government units as the implementation of municipal economy, and even tasks falling within the category of public utility.

A key problem in assessing the admissibility of economic activity appears to be which tasks can be attributed to the general interest and which tasks should be regarded as going beyond the public interest. The notion of public utility, as a generic feature of the municipality's own tasks, means the current and continuous satisfaction of the collective needs of the population through the provision of commonly available services. At the same time, it is important to stress the generality and the need for flexibility in interpreting the affiliation of these own tasks to those related or not related to public utility. In the case of implementation of public utility tasks, the legislator does not limit the choice of forms of implementation of these tasks to local government units, and this rule also applies to counties. Recognising that this is a public utility activity, local government units may use forms appropriate to the public finance sector, such as self-government budgetary establishments or legal forms of companies regulated by the Commercial Companies Code.

As the literature points out, the scale of the concept of general interest […] precludes the possibility of adopting a single, precise significance of the term. Only very general conclusions can be made. […] The use of this phrase is intended to indicate that it is a matter of meeting the needs of society at large. This is the basic meaning of the term, but due to its vagueness it is acceptable to accede other meanings even within the framework of linguistic interpretation (Węgrzynowski, 2012, no. 3: 80–100). Public utility

should be understood primarily in functional terms, in the absence of normative definitions of the concept. Thus, it is necessary to assess whether the activity of the local government falls within the limits of its own tasks and whether it is intended to satisfy the needs of the local community with unidentified characteristics (with the exception of locality). It is therefore necessary to agree on a flexible approach to the scope of public utility, in which the needs of the community should determine the scope of public utility, provided that the expectations of this community are within the scope of activity of local government units. To sum up, in order for a task to be considered a task of general interest, three cumulative conditions must be met. In addition to the requirement to be the local authority's own task, this task has to meet the collective needs of the population on an ongoing and uninterrupted basis. The condition of the universality of the services provided must also be met. Each task which meets the above conditions should be considered a task in the sphere of public utility and should be able to make full use of the available catalogue of forms of performing such tasks (Judziński, 2016, SIP LEX).

Another problem to be clarified is the establishment of the limits of the definition of public utility, because not only can the tasks going beyond the scope of public utility be carried out only by communes and voivodeships, but also the performance of these tasks can only take place in situations and forms strictly defined by law. In a situation where the Act on Municipal Economy goes beyond the scope of public utility, it limits the activity of local government units as to the manner of performing these tasks, allowing only commercial law companies to be used (excluding local government budgetary establishments and other forms appropriate for the public finance sector from the performance of these tasks). The introduction by the legislator of restrictions in the scope of conducting business activity by communes, by defining in particular the legal framework in which it may take place, is determined by the fact that the purpose and sense of the existence of local government are specific public considerations. Conducting economic activity shall not obscure public objectives and excessively absorb the activity of municipalities, whereby not without reason certain public tasks incumbent on the municipalities are connected with organising and creating

conditions for the economic activity of other entities. (From the judgment of the Voivodeship Administrative Court in Olsztyn of 8 September 2011 I SA/Ol 458/11). Therefore, the legislator fears, first of all, that the public entity will not perform the basic tasks imposed on this entity by law, and on the other hand, it does not want to deprive it of its influence on the local market, allowing it to operate beyond the public utility in cases strictly defined by law. The provisions of the Act on Municipal Management and system acts provide for two basic conditions (there are still others) for going beyond the scope of public utility in the case of communes: unsatisfied needs of the self-government community on the local market and unemployment in the commune, which to a large extent adversely affect the standard of living of the self-government community, and the application of other measures and legal measures resulting from applicable regulations has not led to economic activation, and in particular to significant revival of the local market or permanent reduction of unemployment. In the case of voivodeships, it may establish limited liability companies and joint-stock companies and join them if the activity of the companies consists of performing promotional, educational, publishing and telecommunication activities for the development of the voivodeship.

However, the system used by the legislator, is characterised by a certain imperfection, mainly due to the use of vague and notions subjective judgements as if the conditions for going beyond public utility are met. Although in some situations this imperfection can be seen as an advantage, allowing for a flexible approach to the acceptability of commercial activities. Thus, assuming that the task does not fall within the category of tasks of public utility and such a high degree of uncertainty as to the concepts used by the legislator makes it possible, especially for communes, to prove that the economic activity undertaken by them is justified for reasons provided by the legislator.

In conclusion, a number of findings need to be made. First of all, it should be assumed that the municipal economy covers several basic spheres and ranges: the sphere of municipal economy in the strict sense – satisfying the collective needs of the population through the provision of universally available services ("public utility tasks"), intervention on the local economic

market, both for social reasons, as well as for the protection of economic interests of the commune and actions for local and regional development (Kulesza, *Samorząd Terytorialny*, 2012, no. 7–8: 7–24).

Secondly, the scope of municipal management undoubtedly includes the implementation of own tasks and, what is important, not all of these tasks can be included in the sphere of public utility. Thus, there is a sphere of action among the possible activity of a local government unit, which is not aimed at satisfying the collective needs of the community through the provision of commonly available services. This area is strictly regulated by the legislator, both in political regulations concerning particular levels of local government, as well as in the Act on Municipal Management. In support of this assertion, it is worth quoting the fragment of the Supreme Administrative Court's decision cited in the introduction, in which it was stated that not all self-government units' own tasks can be considered public utility tasks. However, when trying to determine which of these tasks should and should not be classified in the sphere of general interest, problems arise in generalizing and constructing a scheme allowing for such categorization, since each situation that raises doubts as to the scope of activity must be considered separately, without losing sight of the context in which the activity is carried out.

The exercise of activities falling within the public service remit shall not be tantamount to activities which exclude profit from those activities, nor shall it be tantamount to obtaining such profit. The activity in the field of public utility is therefore a specific type of tasks of a local government unit, based on satisfying the collective needs of the community. This activity should not be seen in the same way as economic activity, because it is important that not the profit but the implementation of the tasks of the local government unit should be the main objective of this activity.

4 Reasons for undertaking activities outside the scope of public utility

While the general statement that there is a sphere of economic activity going beyond the public utility is clear (since, as previously stated, not every task

can be treated as performed in order to meet the collective needs of the local community), the evolution of the notion of public utility should be assumed. In the judgment cited in the introduction, the main emphasis of the court was on the lack of a basic feature of the activity performed by the self-government unit, which is the ongoing and uninterrupted satisfaction of collective needs. As it is emphasised in the literature, tasks from the public utility sphere should be treated as basic tasks. Tasks of other types may be performed exceptionally, so as not to interfere with the performance of basic tasks (Banasiński, Jaroszyński, 2017, SIP LEX). It is appropriate to recognise the validity of the arguments put forward as a matter of principle, but attention should be drawn to their conservative nature and not taking into account the dynamics of economic and social relations. The need to have an attribute associated with the collective satisfaction of the needs of the community as a legal principle should be treated in a dynamic and undefined way. As it is emphasized in the literature, local government units are subject to the process of evolution. The notion of activity important for the development of the commune should not be identified only with the current, leading function of the commune. In order to enable development of the commune or other local government unit, it is often necessary to take anticipatory actions, which are different from the current profile. Local government units, and in particular cities, are subject to constant change. The potential of the commune (city) is evidenced not only by the quality of its infrastructure, but also by the presence of business entities with well-known and established brands (Gonet, 2010, SIP LEX). Transferring this on the grounds of the arguments raised in the aforementioned judgment, it cannot be ruled out that in view of an open catalogue of own tasks resulting from the political regulations, in favourable circumstances (expectations of the local government community), the own tasks may include those that are normally included in the sphere of interest of commercial entities. The thesis on the changing needs of the community and ipso facto evolvement of the role and tasks of local government units, should be given a fundamental character and its consolidation should be sought, above all, in the practice of the application of law by supervisory authorities and courts. Therefore, when interpreting the system regulations,

as well as the Act on Municipal Management, their interpretation should be based not only on the grammatical wording used, but also on the current expectations of the community, which not only are subjective, but also evolve in the environment of changing social and economic conditions, are far from the realities in which the aforementioned regulations were created earlier.

The conditions for going beyond public utility indicated in the provisions of the Act on Municipal Management become a derivative of the recognition which tasks should be included in the scope of public utility. Only after considering that a particular task cannot be included in this group should we consider whether the law allows local government units to go beyond this sphere. An attempt to determine the limits of economic activity of local government units on the local market. One of the most important prerequisites for engaging in activities falling outside the public interest remit appears to be the related to the financial impact of these activities. Taking up this activity means both potential sources of revenue for the local government budget and the necessity to make budget expenditures, including the losses that this activity may bring. These effects must be determined not only by the size and type of economic activity, but also by the choice of form of this activity. Both the Act on Public Finance and the Act on Municipal Management preclude the use of the form of a self-government budget establishment for the performance of tasks going beyond the public utility, which clearly indicates the need to use forms not included in the public finance sector. Therefore, the leading form of going beyond the discussed scope will be a capital company or, which raises many doubts, a partnership in which a local government unit will participate as a partner.

However, in addition to the potential budget revenues provided by corporate dependencies, attention should be paid to clear benefits of not burdening the public entity with the costs of carrying out its tasks, which is important in particular in terms of commitment of expenditures by entities belonging to the public finance sector. The use of the legal form of limited liability companies (not only to the extent exceeding the scope of public utility), brings the advantage of outsourcing the debt of this entity.

Despite unquestionable benefits of a private law source of income (except for public law ones), local government units should refrain from direct involvement in economic activity, not only because of the risks inherent in economic activity, but also the distortion of competitiveness on the local market, and focus primarily on the function of a regulator and stimulator. Thus, wherever there will be unmet needs of the community, and no private entity will be able to satisfy them, there is an open space for the activities of local government units. However deeper role of the commune (city) engaging in commercial undertakings through the establishment of commercial law companies or joining these companies cannot be ruled out, if only local government bodies are able to justify such activity with the needs of the community, not only related to its direct needs, but also aim at the development of the commune, e.g. by supporting entrepreneurship (Gonet, 2013: 136). The legal right resulting from the provisions of Art. 9 and Art. 10 of the Act of 1996 on Municipal Management cannot be understood in complete separation from the essence of municipal management conducted by local government units. Economic activity going beyond the sphere of public utility should show benefits for the inhabitants of the self-government community, but it should be excluded that this criterion should be met only for the purpose of earning money. Thus, not only an increase in budget revenues, but also other measurable benefits for the local government community.

5 Conclusions

Local government units are primarily public authorities, which means that in order to carry out tasks imposed by law, they have to diagnose the needs of residents in terms of meeting those needs for which the public entity is responsible. However, the role of the public entity is not only to satisfy the materialized needs of the inhabitants by creating a system of municipal services, but also to organize and stimulate positive developments in the local community. This is particularly the case of socially necessary activities in which private operators are not interested in starting up (e.g. because of the low profits from the activity in question), the creation of new jobs, and the promotion and activation of local economic, social and cultural

activities. Referring to the judgment cited at the outset, it should be admitted that banking activity conducted directly by a local government unit (through the establishment of a capital company) may be included in the broadly understood meeting the needs of the local community. Activation of the local community, not only has a positive impact on the standard of living of the inhabitants, but will also result in an increase in public and legal income of local government units. Undoubtedly, this sphere of activity should be preceded by both legal analysis of its admissibility and careful economic analysis taking into account the benefits and possible risks resulting from running a business activity. Commercial activities should be of a temporary nature, i.e. they should be carried out only in the initial stage, i.e. when there is an indication of going beyond the public interest. Once these needs have been satisfied, the local government unit should refrain from engaging in the activity in question.

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Pecuniary Damages from the Commune Budget for a Premises Owner in Case of the Commune's Failure to Provide Social Housing to a Person Entitled to it Following a Court Judgement

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Abstract

The Act on Tenants' Rights, Municipal Housing Stock and the Amendment of the Civil Code provides for statutory liability of the commune in case of failure to provide social housing to a person entitled to it following a court judgement. The purpose of this paper is an attempt to sketch the essential circumstances related to the origins of that claim, the manner in which it can be satisfied, and the potential financial consequences for the budget expenditure of the local government unit.

Keywords: Claim for Damages Towards the Commune; Public Finances; Local Government Unit Budget.

JEL Classification: K30; H72.

1 Introduction

The local governments want to have higher independence. From this reason, local government units try to maximizing revenues. (Franczak, 2018).

Pursuant to Article 18(5) of the Act on Tenants' Rights, Municipal Housing Stock and the Amendment of the Civil Code (TRA) of 21 June 2001,[2] if the commune fails to provide social housing to a person entitled to it following a court judgement, the owner is entitled to a claim for damages towards the commune under the Civil Code of 23 April 1964 (Journal of Laws 2018, item 1025).

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2 Article 417, consolidated text: Journal of Laws 2018, item 1234, as amended.

This paper will discuss issues related to budget expenditures resulting from the damages referred to in Article 18(5) of the TRA. The question will be approached primarily from the perspective of general principles of liability of the commune under the Civil Code[3] of 23 April 1964 (CC), as well as regulations on financial management of local government units, i.e. the Public Finance Act of 27 August 2009.[4]

2 European Union and national law aspects

2.1 The European Union law aspect

Due to the length of this paper, it is not possible to discuss legal regulations of specific EU member states on the issue in question. There are, however, some overarching principles collected in a legal act of a general nature, namely the Charter of Fundamental Rights of the European Union[5], which are addressed to the EU member states. The document has been adopted by the European Parliament, the Council and the Commission.

Since the topic refers directly to protecting the right to property – as it discusses pecuniary damages for breaching the right to disposing of one's private possessions – two articles of the Charter, relevant to the issue at hand, ought to be mentioned: Article 17(Right to property) states that: "*Everyone has the right to own, use, dispose of and bequeath his or her lawfully acquired possessions. No one may be deprived of his or her possessions, except in the public interest and in the cases and under the conditions provided for by law, subject to fair compensation being paid in good time for their loss. The use of property may be regulated by law in so far as is necessary for the general interest.*" This norm is correlated with Article 47(Right to an effective remedy and to a fair trial), which states that: "*Everyone whose rights and freedoms guaranteed by the law of the Union are violated has the right to an effective remedy before a tribunal in compliance with the conditions laid down in this Article. Everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal previously established by law.*"

Putting those two articles side by side, one can presume that member states should guarantee that the right to property is respected in each of its aspects.

3 Consolidated text: Journal of Laws 2018, item 1025, as amended.
4 Consolidated text: Journal of Laws 2017, item 2077, as amended.
5 Official Journal of the European Union, C 326/391.

Undoubtedly, one of these aspects is the right to damages where an entity (such as a commune) fails to perform the tasks it has been obliged to by statute. In such circumstances, these stipulations allow to admit an argument that the aforesaid rights of the citizen must be respected, including through access to judicial proceedings. These EU principles have been manifested in the Act on Tenants' Rights, Municipal Housing Stock and the Amendment of the Civil Code of 21 June 2001 cited in the introduction.

2.2 The definition and judicial origin of the right to social housing in the national law aspect

Before proceeding to analysing specifically the budget expenditures of a commune for purposes related to satisfying the claims referred to in Article 18(5) of the TRA, one should mention other, general legal regulations that grant an entitlement to social housing to specific persons.

Social housing is defined in Article 2(1)(5) of the TRA as premises suitable for residence due to their furnishing and technical conditions, in which the surface of rooms per member of the tenant's household cannot be smaller than 5 square meters, or 10 square meters in the case of a single person household, and the premises can have a lowered standard.

In turn, Article 14 regulates the procedure for granting such premises to persons entitled to them under statute. Article 14(1) states that, in a judgement ordering premises to be vacated, the court rules on whether persons affected by the order are entitled to receive social housing or not. The obligation to provide social housing rests with the commune corresponding to the location of the premised to be vacated. The Act further states that, if the judgement grants the entitlement referred to in Article 14(1) to two or more persons, the commune is obliged to provide to them at least one social housing unit. The court, when examining *ex officio* whether grating the right to receive social housing is warranted by circumstances, rules on the entitlement of persons referred to in Article 14(1), taking into consideration their previous manner of using the premises and their specific material and family situation.

Article 14(4), in turn, lists circumstances in which the court is obliged to grant the right to social housing, stating that the following persons cannot

be refused this right (unless they are able to move to premises other than previously occupied):

- pregnant women,
- minors, persons with disability in the meaning of regulations of the Social Welfare Act of 29 November 1990, or legally incapacitated persons, as well as persons caring for and living together with them.
- persons bedridden on account of illness,
- old age and disability pensioners that meet the criteria for receiving social welfare benefits,
- persons registered as unemployed,
- persons meeting other criteria set out by the commune council by means of a resolution.

When issuing a ruling on the right to social housing, the court orders a stay of vacating the premises until the commune provides an offer to conclude a social housing unit tenancy agreement.

Based on these legal regulations, courts order the eviction of tenants, that is vacating, emptying and handing the premises over to the plaintiff (owner). At the same time, courts rule on entitlement to receive social housing and stay the vacation of premises until the commune provides an offer to conclude a social housing unit tenancy agreement.

A derivative and secondary issue related to enforcing these rulings is the issue discussed in this paper, namely the payment of damages by the commune (budget expenditure) in case of failure to provide social housing to a person entitled to it following a court ruling referred to above.

2.3 Claim for damages towards the commune – voluntary payment versus payment following a court ruling

The literal wording of Article 18(5) of the TRA says that it is the commune that bears the economic (financial) burden of failing to provide social housing to an entitled person. Doubts can, however, arise as to the manner in which this claim is to be satisfied by the commune: through mutual amicable agreements with the property (premises) owner or through the court awarding the relevant amounts from the commune to the property owner. The cited article does not regulate this issue, although it appears quite

reasonable that the commune can fulfil its duty in either of the two ways named above. An amicable agreement has both advantages and disadvantages. It certainly allows settling the matter quickly and eliminating uncertainty between parties to the dispute, and also avoiding additional judicial costs, which has a bearing on the commune's financial capabilities. On the other hand, however, the view taken on the matter by the court, and in particular by court experts dealing with property assessment, is far from certain. In effect, the damages awarded by the court may be significantly lower than if they were amicably agreed by the parties through negotiations.

For these reasons, no unequivocal answer can be given as to which option should be favoured. However, the specificity of judicial proceedings merits a more detailed discussion.

2.4 Compensatory claim towards the commune – satisfaction in judicial proceedings

As noted above, judicial proceedings are one of the ways of enforcing claims against a commune that failed to provide social housing to a person entitled to it following a court judgement. The cited Article 18(5) of the TRA refers, however, to Article 417 of the CC, which it turn states that liability for illegal acts or omissions while exercising public power is borne by the State Treasury, local government unit or other legal person exercising such power by virtue of law. If the exercise of public power tasks has been entrusted by means of an agreement to a local government unit or other legal person, both the entrusting local government unit or State Treasury and the contracting entity bear joint and several liability for damage caused.

A court judgement[6] states that a claim under Article 417(1) of the CC in connection with Article 18(5) of the TRA should be interpreted on an individual but special basis, because the owner, due to an omission of the commune, cannot fully enjoy his or her right to property, and said Article 18(5) of the TRA is meant to protect the interests of housing owners as the 'weaker' party compared to the commune.

6 Judgement of the Włocławek District Court of 31 March 2017 (file ref. no. I C 2372).

It must be noted that, in order for the commune to become liable on this account, the following circumstances must arise:

- damage suffered by the property owner,
- an illegal act or omission of the commune in exercising public power,
- a causal connection between the damage and conduct of the commune.

In addition, judicial decisions emphasise that these circumstances must be fulfilled jointly (cumulatively). As an example, a ruling of the Białystok Court of Appeal[7] stressed that: "*The circumstances listed in Article 417 of the Civil Code must arise cumulatively, which means that failure to demonstrate at least one of them invalidates the entire claim for damages founded on that article. The burden of proof in this respect is on the plaintiff.*" In turn, another court ruling[8] notes that: "*For liability for tort under Article 417 of the CC to arise, the necessary circumstance is the illegal nature of the act or omission of the authority exercising public power, which must be proved by the plaintiff according to the general burden of proof placement principles (Article 6 of the CC).*" The above then shows unquestionably that it is the plaintiff (property owner) who needs to demonstrate all these circumstances.

To demonstrate his or her entitlement for damages, the owner may refer to Article 140 of the CC. The legal norm found therein states that, within the limits set by statute and rules of social conduct, an owner may, to the exclusion of others, use a thing in accordance with the social and economic purpose of their right, and in particular collect the proceeds and other revenues from said thing. The ability to use and dispose of property cannot be questioned. The specific nature of this regulation is often examined by Polish courts. By way of example, a judgement of the Warsaw Court of Appeal[9] noted that Article 140 of the Civil Code, by expressing the essence of ownership, contains a two-pronged definition of this right, corresponding to its positive and negative aspects. The court stressed that: "*The positive aspect is meant to consist in the entitlements that make up the right*

7 Judgement of the Białystok Court of Appeal of 28 September 2017 (file ref. no. I ACa 289/17).

8 Judgement of the Warsaw Court of Appeal of 15 March 2017 (file ref. no. I ACa 2124/15).

9 Judgement of the Warsaw Court of Appeal of 20 June 2017 (file ref. no. I ACa 577/16).

of ownership as a subjective right, while the negative aspect means the owner's ability to exclude other persons from entering into the sphere of his or her right. The entitlement of the owner to use and dispose of a thing is therefore accompanied by the obligation to refrain from any interference, while providing the protective remedies which the owner can utilize against the party in breach."

In this context, it should be assumed that the owner's inability to use the property in these circumstances is caused solely by the commune's failure to provide social housing to a person entitled to it. The owner cannot arbitrarily remove the tenant from his or her property, the eviction judgement preventing him or her from doing so due to the legal justification found in Article 14(6) of the TRA. As a reminder, the article states that, when issuing a ruling on the right to social housing, the court orders a stay of vacating the premises until the commune provides an offer to conclude a social housing unit tenancy agreement.

Consequently, it can be concluded that such conduct of the commune will be illegal, since pursuant to Article 14(1) of the TRA the obligation to provide social housing rests with the commune corresponding to the location of the premises to be vacated. As emphasised in a Supreme Court judgement,[10] a final judgement granting a right to social housing has the consequence of imposing an obligation to provide such housing to the entitled person on the commune. The Supreme Court also pointed out directly that one of the criteria for the commune's compensatory liability is the illegal nature of the failure to fulfil the obligation. In another ruling[11] (file ref. no. V CK 253/03), the Supreme Court stressed that a commune's liability on that account does not depend on demonstrating the fault of the commune; on the contrary, the basis for a compensatory claim towards the commune is the very fact of failing to provide social housing to a person entitled to it following a court judgement. The above considerations lead to a conclusion that, in similar situations, the criterion of illegal omission of the commune while exercising public power will be met.

10 Judgement of the Supreme Court of 13 May 2015 (file ref. no. V Ca 1/15).
11 Judgement of the Supreme Court of 18 February 2004 (file ref. no. V CK 253/03).

2.5 The twofold nature of damages – lost profits and actual losses

Since the commune's liability in the above scope is basically a foregone conclusion, it remains for the law to discover the meaning of the wording "claim for damages" as used in the statute.

However, by way of an introduction, a mention should be made of positions taken by legal doctrine with regard to this material scope. In the already mentioned commentary (dr hab. Osajda K (ed.), art. 18, Ustawa o ochronie praw lokatorów mieszkaniowym zasobie gminy i o zmianie Kodeksu cywilnego) to Article 18 it is noted that: "*A reference to Article 417 of the CC allows owners of the premises to demand damages from the commune in the full scope set out by Article 361 of the CC (cf. the decision of the Supreme Court of 25 June 2008, III CZP 46/08, Legalis). In a resolution of 16 May 2012 (III CZP 12/12, OSNC 2012, no. 12, item 138), the Supreme Court stressed that losses consequent upon the inability to obtain lease rent and losses resulting from the owner having to bear the costs of using the premises, including amounts due for water, electric energy and heating, on his or her own, may remain in a normal causal relationship (Article 362(1) of the CC) with the commune's failure to perform the obligation to provide social housing to an entitled person (for more on adequate causal relationship in cases of failure to provide social housing see: K. Damasiewicz, Gloss to a resolution of the Supreme Court of 16 May 2012, III CZP 12/2, Legalis).*" Further, it was also stressed that: "*In light of the above, it should be stated that the loss of the owner may consist in either sustaining expenses related to using the premises by a former tenant, or not obtaining (losing) rent. They are both forms of property loss which must be demonstrated and remain in a normal causal relationship with the failure to fulfil the obligation to provide social housing (now: obligation to provide social housing to a person entitled to conclude a social housing unit tenancy agreement) by the commune.*"

The above views set out the structure (constituents) of the aforesaid claim for damages. The damage suffered by the owner can be considered as consisting of two constituents, namely the already sustained expenses related to the tenant's use of the premises and the expected benefits which the owner failed to achieve due to his or her inability to dispose of the premises. In this respect, one may speak of damage in the sense of, respectively, actual losses and lost profits.

Based on this legal distinction, a judgement of the Katowice Court of Appeal[12] states that: "*The provision of Article 361(2) of the CC shows that a loss encompasses the actual loss as well as lost profits. The loss is evidenced in the actual change of the property situation of the injured person and consists either in a decrease of their assets or an increase of their obligations. Lost profits mean those assets of the injured person's property which would have materialized if not for the event that caused the loss. Loss in the form of lost profits cannot be entirely hypothetical, but must be proved by the injured party with probability so large that, under common sense reasoning, the loss of expected profits can be reasonably admitted.*"

The legal possibilities of the owner pursuing damages for such kind of loss need to be assessed separately. In case of lost profits, this may be primarily the unrealized rent for leasing the premises. An owner pursuing such claim against the commune must, however, demonstrate that he or she would obtain specific income from a lease agreement if such premises were occupied by a tenant. This means that the burden of proof referred to in Article 6 of the CC (the burden of proving a fact rests with the person who uses the fact to derive legal consequences) is on the owner. The aforesaid regulation contains one of the principal rules of civil proceedings, whose importance has many times been emphasised in judicial decisions. As an example, a judgement of the Katowice Court of Appeal[13] stresses that: "*The provision of Article 6 affords a general conclusion that subjective rights may be effectively pursued insofar as a party is able to demonstrate facts used to support statements advantageous to it. The court should, therefore, accept facts proved by the party bearing the burden of proof as true and disregard others which were not convincingly demonstrated. It should also be considered that the court must rule on the essence of the case even if evidence discovery was ineffective; in such case, the court should rule against the party that based its claims on unproven facts. These rules apply in civil proceedings.*"

The above, therefore, shows that the property (premises) owner must absolutely demonstrate his or her claims related to lost profits. In practice, this obligation should be fulfilled by producing relevant evidence. Undoubtedly, the most suitable method would be to rely on the opinion of a court expert dealing in property assessment, who is able to analyse market lease prices and

12 Judgement of the Katowice Court of Appeal of 9 March 2017 (file ref. no. I ACa 1002/16).

13 Judgement of the Katowice Court of Appeal of 30 August 2018 (file ref. no. I ACa 72/18).

demonstrate the profits lost by the owner in a specific timeframe. It should be noted that, in this material scope, only a claim that is amply supported by evidence stands a chance to be accepted by the court.

The other form of loss, i.e. the expenses actually sustained by the owner to maintain the premises, can likewise be compensated by a court ruling, although in this case they are referred to as "actual loss". As far as actual loss is concerned, it may comprise different kinds of costs, including but not limited to service charges not paid by the tenant (and paid by the owner). Since such costs are borne by the owner, his or her assets are subject to decrease. Consequently, actual economic damage arises that needs to be compensated by awarding suitable amounts by a court ruling.

2.6 The moment triggering the compensatory liability of the commune

Even though this issue has not been regulated in legal provisions, a suitable answer can be found in judicial decisions. The decisions show unequivocally that such liability does not arise automatically but depends primarily on the moment when the commune learned about the contents of the eviction judgement that granted the right to social housing.

Consequently, all pecuniary claims advanced during judicial proceedings but not made known to the commune earlier through mandatory notification will be disregarded in the court ruling. Such arguments made the Iława District Court[14] dismiss the suit for damages pursuant to Article 18(5) of the TRA, brought by a property owner. A similar logic was used in a Łódź Regional Court judgement.[15] In the latter judgement, it was stressed that, since the deadline for fulfilling the obligation to provide social housing depends on the initiative of the person entitled to social housing who is named in the body of the enforcement order or his or her creditor, the obligation itself is of indefinite duration, since no deadline has been defined by statute, court judgement or nature of the obligation. Pursuant therefore to Article 455 of the CC, this obligation should be performed immediately after calling the commune, as the debtor, to provide social housing

14 Judgement of the Iława District Court of 25 August 2015 (file ref. no. I C 773/15).
15 Judgement of the Łódź Regional Court of 29 May 2015 (file ref. no. III Ca 237/15).

to the eligible person. The word "immediately" should, in fact, be considered realistically, considering all the circumstances of a particular case. Further, the justification states that: "*In the discussed case, it was undisputed that the plaintiff called the defendant City of (…) to provide (…) an offer to conclude a social housing unit agreement only by a letter of 10 March 2012 and therefore the period to fulfil the discussed obligation by the City of (…) commenced to run on the date of serving that letter to the defendant. Consequently, it should be assumed that the plaintiff's claim for awarding damages for failure to provide social housing in the period from 15 October 2008 to 18 March 2012 was not due (…).*"

Finally, one should mention the position expressed in a judgement of the Gdańsk Court of Appeal[16] which stressed that notifying the commune about the contents of the eviction judgement granting the right to social housing is a trigger for the commune's liability, since it informs the commune that providing social housing to the evicted person is necessary.

The above judgements thus provide another clue to the property owner, who must observe the aforesaid procedural requirement to have a realistic expectation for his or her claim to be awarded by the court. On the other hand, the commune can use these judgements to question the owner's suit on procedural grounds.

2.7 The manner of satisfying the claim for damages in light of the Public Finance Act

The aforesaid aspects of pursuing damages from the commune should also be assessed in the perspective of principles found in the Public Finance Act. While the act does not, obviously, require from the commune any specific manner of action as regards fulfilling its statutory duties, some guidelines found in these regulations can be helpful. In this respect, particular reference can be made to Article 44(3), which states that public expenditures should be made in a purposeful and cost-effective manner, while observing the following principles:

- obtaining the best results from particular inputs,
- ensuring optimum choice of methods and means for achieving the set objectives.

16 Judgement of the Gdańsk Court of Appeal of 27 May 2014 (file ref. no. V ACa 505/13).

Importantly, these general guidelines are addressed to, among others, communes. The regulation uses the term "public expenditure", and such status is assigned to the aforesaid damages. In the same legal norm, utility and cost effectiveness, together with the optimum choice of methods and means for achieving a specific objective, were highlighted as the key issues in expending budget resources.

Using these assumptions, the commune should make its own decision as to which option is more advantageous. The commune must therefore choose whether to voluntarily enter into active negotiations with a particular claimant owner, or leave the claim to be examined by the court. Both options have their advantages and disadvantages.

For out-of-court agreements, important factors undoubtedly include the rapid resolution of dispute and lack of exposure to additional costs (except for damages paid) such as court costs and attorney fees. It should be stressed that such additional, unplanned costs may significantly increase the commune's budget expenditures. For example, bringing a suit to the court means that the owner must pay a court fee set forth in the Act on Court Costs in Civil Cases of 28 July 2005 (Consolidated text: Journal of Laws 2018, item 300, as amended) which may vary depending on the manner in which the suit is brought. As a general rule, in cases involving property a relative fee is collected, equal to 5 % of the value of the object of dispute or object of complaint, not smaller however than PLN 30 and not greater than PLN 100 000. Alternately, the owner can initiate writof payment proceedings, where the fees are lower. Regardless of the path chosen, the fee can increase the final cost of judicial proceedings by an amount ranging from a few hundred to a few thousand zlotys, depending on the value of the object of dispute.

Irrespective of this, an owner who enlists the help of a professional attorney bears the costs referred to in the regulation of the Minister of Justice of 22 October 2015 on fees for the actions of legal counsels (Consolidated text: Journal of Laws 2018, item 256, as amended). In the regulation, minimum fees of these counsels have been set. For example, when the object of dispute is valued between PLN 10 000 and PLN 50 000, the minimum fee is PLN 3 600 (PLN 2 400 in writ of payment proceedings). Importantly,

if the owner's claim is granted by the court, all of these costs will be borne by the commune.

Ultimately it may turn out that costs related to judicial proceedings will in themselves be a significant burden for the commune's budget. On the other hand, the judicial proceedings stage allows the commune to actively question the owner's claims in different ways, including procedural ones.

In summary, the optimum course of action for the commune cannot be determined in advance. It appears that actual circumstances of the case will play a key role. Finally, it should be added that giving the commune a free hand in choosing the manner in which this budget expenditure will be made is also supported by systemic solutions found, among others, in the Commune Local Government Act of 8 March 1990 (Consolidated text: Journal of Laws 2018, item 994, as amended) especially in the provisions of Article 2(1) thereof which states that the commune performs public tasks in its own name and on its own responsibility. In practice, a conclusion may be drawn that the commune, as a local government unit independent and separate from government bodies, should be granted discretion to decide on the forms and methods of performing its own tasks. As far as the commune budget is concerned, the above article is complemented by Article 52(1) which states that the commune manages its finances on its own, based on a budget resolution.

3 Conclusion

Each commune has to face claims advanced by owners under Article 18(5) of the TRA, and must therefore set aside certain means to satisfy these obligations in its budget expenditures. The manner in which the obligation is performed (in or out of court) is left to the discretion of the commune due to its political autonomy. In this respect, the commune should consider primarily arguments resulting from the principles of managing public funds listed in the Public Finance Act, since the good of public finances is the overriding value.

As mentioned in the introduction, the Charter of Fundamental Rights of the European Union is of particular importance for satisfying similar claims

of property owners based on the legislation of member states. Obviously, this document defines only the general legal framework in this material scope, but at the same time provides important legislative assumptions for EU member states.

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REPORT

The V International Conference on Financial Law "The Financial Law towards Challenges of the XXI century"

Tomasz Sowiński[1]

Department of Financial Law, Faculty of Law and Administration, University of Gdańsk (Poland), "The Gdansk University Center for Self-Government and Financial Law" (hereinafter – the Center), (Poland), Regional Chamber of Audit in Gdańsk (Poland), Department of Financial Law and Economics, Faculty of Law, Masaryk University in Brno (Czech Republic) and Department of Financial and Tax Law, Faculty of Law, Pavol Jozef Šafárik University in Košice (Slovakia) jointly organised the 5th International Baltic Conference on Financial Law entitled "The Financial Law towards Challenges of the XXI century" which took place during a cruise across the Baltic Sea and on the island of Öland on 10–13 May 2019.

The research project "The Financial Law towards Challenges of the XXI century" is a continuation and development of a project with the same name from years 2009–2017. This project was an object of great interest and was warmly accepted by scientific communities associated with financial law and economics in Poland, Lithuania, Czech Republic, Slovakia, Ukraine and Russia. The Center in cooperation with the Department of Financial Law, lead the project. The idea is to have a transparent scientific outcome for knowledge transfer: from research to policy and practice. We realise this project also through a cooperation with the Regional Chamber of Audit in Gdańsk. The proposed project topics included issues regarding financial law and public finance, local government financial law, tax law, insurance law, the law of financial markets and international financial law. Due to the nature of the research project, it was necessary to develop proposals de lege lata and/or de lege ferenda relating to research, in the context of 21st century challenges of financial law.

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The Program Council, which supervised the high scientific level of the conference, consisted of:

- Prof. zw. dr hab. Jolanta Gliniecka, Poland
- Prof. zw. dr hab. Jerzy Gwizdała, Poland
- Prof. zw. dr hab. Jadwiga Glumińska-Pawlic, Poland
- Prof. zw. dr hab. Elżbieta Kornberger-Sokołowska, Poland
- Prof. UWM dr hab. Mariola Lemmonier, Poland
- Prof. WSB doc. JUDr. Petr Mrkývka, Ph.D., Czech Republic
- Doc. JUDr. Ing. Michal Radvan, Ph.D., Czech Republic
- Prof. h. c. prof. JUDr. Vladimír Babčák, CSc., Slovakia
- Prof. h. c. doc. JUDr. Mária Bujňáková, CSc., Slovakia
- Prof. Dr Marina V. Sentsova, Republik of Russia
- Luiza Budner-Iwanicka, President of RIO in Gdańsk, Poland
- Dr Tomasz Sowiński, Head of the Center PSiPFL UG, Poland

The conference was organised by a local organising committee composed of:

- Dr Tomasz Sowiński – conference manager
- Dr hab. Edward Juchniewicz – deputy manager
- Dr Anna Drywa – deputy manager
- and all employees of the Department of Financial Law at the Faculty of Law and Administration, University of Gdańsk.

On behalf of our partners, the coordinators were Luiza Budner-Iwanicka (RIO Gdańsk), Eva Tomášková (Masaryk University in Brno), and Anna Románová (Pavol Jozef Šafárik University in Košice).

It is more than necessary to thank Prof. Jolanta Gliniecka, head of the Department of Financial Law at the Faculty of Law and Administration, University of Gdańsk, Prof. Petr Mrkývka, head of the Department of Financial Law and Economics at the Faculty of Law, Masaryk University in Brno, for their kindness and invaluable help. The organisers would also like to thank Prof. Vladimír Babčák, head of the Department of Financial and Tax Law, Faculty of Law, Pavol Jozef Šafárik University in Košice, Mrs Luiza Budner-Iwanicka, President of Regional Chamber of Audit in Gdańsk, and *Prof. Marina* Valentinovna *Sentsova*, Voronezh State University.

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The organisers would like to especially thank their patrons and patrons of the conference: His Magnificence prof. dr hab. Jerzy Gwizdała, Dean of the Faculty of Law and Administration, prof. dr hab. Wojciech Zalewski, President of the Regional Chamber of Audit in Gdańsk. We further thank the President of the City of Gdańsk, Mrs Aleksandra Dulkiewicz, for her patronage and support. We would also like to thank the Pomeranian Bar Association in Gdańsk and the owners of the Ziaja brand celebrating its thirtieth anniversary. We should also kindly mention our social partners. The Association of Vistula Cities, a non-governmental organisation created by 22 cities – local government units, is with us through all conferences. Additionally, ZMN, in close cooperation with other non-governmental organisations, including those created by local government units of various levels and types, provided us with the opportunity to cooperate with hundreds of local government units, including regions from many countries of the Baltic Adriatic Transport Corridor.

The main objective of the Center for Local Government Law and Local Financial Law is primarily the realisation of its projects. It also develops projects in cooperation with other academic and non-academic partners, public and private institutions, non-governmental organisations and others, whose aims are coherent with the aims of the Center. The Center cooperates with domestic and foreign scientific and didactic institutions, offers specialist courses and lectures on self-government law and local financial law. It participates in the organisation of scientific and research meetings promoting scientific research as well as consulting services. One of the essential forms

of the Center's activity is initiating and supporting various publishing undertakings which integrate the scientific society. It has already organised several international scientific conferences and seminars, moreover, issued many publications – mostly of an international character. The Center is also the publisher of the Financial Law Review academic quarter (FLR), which is a scientific magazine published in English in electronic form. To promote FLR and to show its scientific potential during the 5th International Baltic Conference on Financial Law "Financial Law towards Challenges of the XXI century", the Centre's scientific magazine organised the 1st International Seminar of Financial Law.

During both scientific events, i.e. the 5th International Baltic Conference on Financial Law and the 1st International Seminar of Financial Law, a group of more than 100 participating scientists from 7 countries presented the results of its work as well as cooperation of many entities; universities, faculties of law and financial law from several countries and many years of experience. Altogether two scientific sessions, ten conference panels and three panels of the FLR seminar took place during both events, culminating in a joint session summarising the entire scientific work. During the final session, all moderators of Conference and Seminar sessions and panels presented a summary, and then, as after each session, a panel discussion was held for all participants of both scientific events.

During the 1st plenary session of the 5th International Baltic Conference on Financial Law "Financial Law towards Challenges of the XXI century" which was moderated by Prof. Jadwiga Glumińska-Pawlic, lectures were delivered by five participants. Prof. Hanusz presented the issue of financial law's place in the system of Polish law. Dr Eva Tomášková described the evolution of public finance in the Czech Republic, and Dr Romana Buzková presented the cohesion policy in the light of public finance. Prof. Imeda Tsindeliani raised the issue of public finance and public financial law institutions in the context of digital economy development. The President of the Regional Chamber of Audit in Gdańsk, Mrs Luiza Budner-Iwanicka, acquainted the conference participants with the history of 25 years of regional accounting chambers in Poland, presenting the balance of functioning of the supervisory and control institutions over

the financial economy of local government units. The plenary session ended with a discussion of participants.

During the next thematic scientific panels, the following issues were discussed: tax law, international tax law, VAT – selected issues, financial law in the European Union, financial law of the local government, financial law of the Russian Federation, and during the 1st International Seminar of the Financial Law Review, general issues of financial law and the financial market.

Prof. Vladimír Týč moderated the panel on international tax law, and according to his report, it had the following course. In line with the title of the Conference, all contributions were devoted to current new problems of tax law. The title of the panel "International Tax Law" was not followed literally, but panel participants could hear contributions dealing with international or European aspects of tax law or with specific problems of some of the participating countries linked to latest developments of the tax regulation. To start with the international element, the contribution of Dominik Gajewski (Poland) "Treaty shopping jako instrument w międzynarodowej optymalizacji podatkowej" analysed the phenomena of treaty shopping – how to use (and abuse) bilateral double-taxation agreements. Following speakers pointed out new phenomena of the world of taxes: Petr Vodák (Czech Republic) spoke about the "value creation as the new taxation standard in the global digital economy" and Michal Radvan together with Zdenka Kolářová (Czech Republic) addressed the problem of Airbnb taxation, so far not regulated by tax law. Another group of speakers reported on the experience with specific national problems in a very inspirational way for other countries. A broader context of the tax law was addressed by Dmitry Artemenko (Russian Federation), who was speaking about the development of tax criminality in his country and the fight against it, using interesting statistical data ("On the issue of tax crimes"). Marie Karfíková and Hana Marková (Czech Republic) in their contribution entitled "New trends in the development of the tax system and their impact on the budgetary system of the Czech Republic" outlined how to make the tax system more efficient taking into account budget requirements, evaluating the Czech experience. Dariusz Strzelec (Poland) examined selected problems on the application of rules concerning the supervision in the field of taxes and

customs ("Application of the provisions on customs and fiscal control"). The entirety of all contributions reflected current problems of tax law, and consequently, they were very useful, informative and inspirational for all participants. We can reach the conclusion that tax law is developing fast in all countries and requires the evaluation of the current regulation and practice and mainly the future development, that must modify current tax law institutes or adapt them to new conditions. The development of tax law is an endless process since the progress cannot be stopped. All presented topics should thus be further elaborated in future.[2]

Prof. Patrycja Zawadzka moderated the panel on tax law, and according to her report, it had the following course. Six papers on tax law were presented. The first of the papers "The evolution of taxation of wind farms in Polish and French tax law" was delivered by prof. UWM dr hab. Bogumił Pahl and dr Michał Mariański. The speakers presented the changes that have taken place in the tax law of both countries in an exciting way. Based on the analysis of over 140 judgments of Polish courts, the lack of tax stability in the scope of taxation of wind farms was indicated. Examples of problems with the taxation of dock structures and non-contact car washes were also presented. The part devoted to the French General Tax Code and wind farm taxation methods adopted in France also met with great interest. The second speaker was Dr Jozef Sábo, who delivered a paper on "New ways for evaluation of evidence in tax matters". In his speech, he presented basic assumptions in the field of tax records, the burden of proof, methods to eliminate doubts in the field of tax evidence and the so-called profiling. The speaker focused on the normative and descriptive approach to evidence, which was distinguished at the beginning of the 20th century by American lawyer John H. Wigmore. The distinction between statutory requirements for the admission of specific evidence and the so-called factual findings during tax proceedings (e.g. drawing an expert opinion) was presented then. Afterwards, special attention was devoted to the methods of Wigmore charts. The speaker familiarised the audience with the essence of charts and selected interesting facts about the data contained in them. He pointed to the resulting efficiency, predictability and uniformity. The third speaker

2 Based on the report of Prof. JUDr. Vladimír Týč, CSc.

was Dr Łukasz Karczyński, who delivered a paper on "Judiciary law-making and tax imposition in a statutory law system. A Polish example." In his presentation, he presented the research results based on the analysis of the case-law of Polish courts. The importance of court ruling lines for applying tax law and three basic types of judicial lawmaking were emphasised.

Doc. JUDr Miroslav Štrkolec, Ph.D. delivered a paper on "Insurance tax in Slovakia." It presents the concept of insurance tax law, the development of legal regulations on insurance taxation in Slovakia, with particular emphasis on the property insurance category. The speaker also presented interesting results of his research in the area of taxes in the Member States of the European Union. Mrs Agata Lipińska gave a presentation on "Tax and balance sheet effects of separation of income sources in corporate income tax." The presentation described the relationship between balance sheet law and tax law. When considering corporate income tax, special attention was paid to capital gains. Participants were interested in examples from the practice of applying the law in the studied area. Dr Szymon Kisiel gave a speech on "Taxation of Banking Sector – Selected Issues." The speaker comprehensively discussed the essence of the tax on financial institutions, whose assumptions were a response to the global financial crisis, initiated by the collapse of the subprime credit market in the United States in 2007. Ratio legis of the tax on certain financial institutions was to strengthen the stability of the financial sector and reduce its occurrence risk. In Poland, however, the funds from the tax on some financial institutions are the income of the state budget and are allocated to current expenses. All of the presented papers met with great interest of panel participants, which was reflected in an ardent discussion. Inspirational issues of the speeches were also the basis for further lobbying conversations.[3]

Prof. Artur Mudrecki moderated the panel on financial law in the European Union, and according to his report, it had the following course. In the first paper entitled "Subsidies in the light of European Union law", Prof. Andrzej Drwiłło pointed out that subsidising supports unfair competition. Anti-subsidy procedures are triggered when there is damage to the Union

3 Based on the report of dr hab. Patrycja Zawadzka, prof. nadzw. UWr, Katedra Prawa Finansowego, Wydział Prawa, Administracji i Ekonomii UWr.

industry, there is a causal relationship between the subsidy and the damage, and the European Union's interest speaks for it. In these cases, compensatory measures are initiated, among others, additional duty and provisional duty. Besides, the party may agree to increase prices for products. Dr Anna Reiwer-Kaliszewska pointed out the lack of definition of subsidies in the European Union regulation and the lack of regulations regarding subsidies in agriculture. Also, EU regulation does not include services. In next speech, Dr Marcin Tyniecki drew attention to the concept of a financial act in the financial law of the European Union. The author of the paper isolated the features of a financial legal act, including coercion, intentionality, the imperative nature of legal norms. Then he pointed to parametric and planned standards. He also made a typology of European Union financial legislation for regulatory and planning (strategic) acts. Petr Mrkývka and Johan Schweigl pointed out issues related to public finances and European Union financial assistance funds. Johan Schweigl emphasised that the European Union and the national authorities of the Member States took steps to stabilise the public finances of some countries in terms of funds and mechanisms for financial assistance in recent years. Attention was paid to the role of the European Monetary Fund, which currently shapes the issues of the theory of financial law and public finance. Dr Małgorzata Wróblewska devoted her speech to discriminatory taxation as a barrier to the free movement of goods under the law of the European Union and the World Trade Organization. The lecturer described product similarity tests using tests on the example of alcohol. Master Arkadiusz Klusek presented a paper on the topic of Programs and guidelines, the nature of these legal acts during the distribution of European funds in Poland. In his speech, he emphasised that acts of internal law specify the rights and obligations of applicants and beneficiaries of European Union programs. After the lecturers' speech, a lively discussion on the issues raised took place.[4]

In the report from "Tax Law – Legislation and General Issues" panel, Prof. Michal Radvan writes that the panel was mainly focused on tax law design and drafting. Leonard Etel and Mariusz Popławski are participating in the group responsible for preparation of the new Polish Tax Ordinance. During this difficult work, they have gained a lot of experience, which was obvious

4 Based on the report of dr hab. Artur Mudrecki prof. ALK.

from their presentation. The topic of reducing the costs of tax procedures in the new Tax Ordinance Bill represents one of the main principles of tax administration – the principle of effectiveness. Etel and Popławski believe that the introduction of the new Tax Ordinance will contribute to reducing the costs of tax procedures in Poland. Nowadays, these costs are too high, which results from excessively formalised and extended procedures of tax and fee collection. The net tax revenue is lower than expected and/or presumed. Authors presented several interesting approaches on how to reduce tax procedure costs. They believe that there should be set a minimum amount when the tax is not collected at all (as there are still some and probably higher costs to collect the tax). They suggest the minimum tax of 50 PLN. However, in this case, some charges and taxes in the Czech Republic would never be paid (e.g. Tax on the immovable property). Prof Radvan strongly agrees that the right ways are electronisation of tax procedure, amendments concerning the delivering of tax decisions and other documents from the tax office to the taxpayer, and especially self-application as a specific matter in the tax law method of regulation. In every case, reducing the costs of tax procedures would contribute to a tax revenues growth supporting the state budget and local government units' budgets. The other member of the group responsible for preparation of the new Polish Tax Ordinance Rafal Dowgier presented the issues of joint and several liability in tax law in connection with the draft of a new Polish codification of general tax law. Dowgier depicts legal solutions referring to chargeability and fulfilment of joint and several tax obligations. The complexity of the discussed subject matter justifies a broader analysis of not too extensive set of provisions related to joint and several liability in tax law. All the recommendation and amendments should follow the principles of effectiveness and economy in tax administration.

Yulia Gorosh focused on issues in the codification of tax law as exemplified by EU-members and post-Soviet non-EU countries The moderator stated that he considered the debates on the position of tax law in the legal system very interesting, also appreciates the attempts to define the "Code" and the necessity and usefulness of tax codes. The crucial question seems to be the decision what is to be codified? The general part of tax law? Procedural tax law? Substantive tax law? Do we really need any codification?

Gorosh believes that to codify tax law, it is necessary to provide internal unity of the system of law and the system of legislation. She prefers to regulate tax procedures by the norms of procedural tax law exclusively, to differentiate them from the norms of the administrative process. She would like to unite the procedural tax norms into a consolidated legal act.

Anna Drywa identified Polish tax culture. In her presentation, she characterised the Polish tax culture analysing the cultural determinism of establishing and applying the law and the legal awareness of taxpayers. According to the moderator (and with simplification) there are countries with a culture of paying taxes (Scandinavian countries) and countries where the heroes are those who avoid taxes and other paying fair taxes are stupid (Poland, Czech Republic, Italy, Greece, etc.). Francesco Cannas was dealing with the taxpayer's rights in the era of de-offshoring, focusing on the case of the exchange of information. The exchange of information is a conditio sine qua non for the proper and fair tax administration in the globalised world. While the State should have the right to get adequate information to assess the tax, the taxpayers have their rights to be protected. An important question is whether the taxpayer should be informed when the tax administration investigates the tax case and in what stage. Szymon Obuchowski informed about the incompletely theorised arguments and their significance in tax law legislation. From his presentation, the importance of the state's right to collect taxes has become clear. At the end, there was an important conclusion that taxes are the politicum. Krzysztof Cień was discussing the tax relieves in the tax planning process and made several remarks on the law as it stands and the law as it should stand. He defined the tax relief, tried to answer why there are so many tax relieves in the tax law, why some tax relieves are obligatory while other voluntary. It is important to know what the role of tax administration is while dealing with (voluntary) tax relieves; shall it apply these relieves automatically?

In the opinion of prof. Radvan, the panel of tax law design and drafting was one of the most important and interesting ones at the conference. All authors professionally presented their research findings and opened the discussion that is definitely not over. The tax law is a living branch of law. The tax law regulation must be able to react to economic and social development in the world and in each country. The sad fact is that the tax law regulation is being prepared

at the ministries of finance by professionals. The draft acts are being discussed by the other experts: tax advisors, university professors, lawyers. It goes through the reviews in the legislative councils. However, the final version is adopted in the Parliament by laics – politicians who have a feeling that they are professionals as they pay taxes. Let's wish they would do the same as their predecessors at the beginning of the 20th century: either they have passed the draft without changes or rejected it. If they continue in practice adopting many changes to the primal draft, the "Christmas tree" model must be applied, as the Czech Ministry of Finance uses: the draft is prepared as "a tree" and the MPs are expected to decorate it with "balls", i.e. tax relieves.[5]

An important and extensive element of the conference were issues related to the financial law of local government units. It was a panel "Financial Law of the Local Government" with the largest number of participants, moderated by Dr Michał Mariański. Eight lectures were conducted during the panel. It is essential to underline that every presentation was strictly part of the research scope defined for this session and concerned finances of local government units. However, this panel can be divided into three main parts. The first part concerned doctrinal problems presented from the perspective of the Polish legal system (presentations of Prof. E. Feret, Prof. M. Augustyniak and Dr R. Kowalczyk). The second part concerned the analysis of selected decentralised finance challenges from the perspective of legal regulations of the Russian Federation (presentations of Prof. E. Chernikov and Prof. E. Kireev). The third part was marked by the speeches of employees of the Regional Chamber of Audit, which confirmed the legitimacy and unprecedented empirical value of the previous considerations (speeches of M. Kopowicz and A. Śróbkowska, R. Fandrejewski and M. Kujawski, and M. Nagórek). The first speaker of the session was Professor Elżbieta Feret, who presented the fundamental thesis of her research relating to the privatisation of public tasks as an opportunity for decentralised actions of local government units. By providing many practical examples to support her deliberations, in particular, the professor reflected on the idea of decentralisation of public finances – wondering if within the new tasks local self-government units receive an adequate implementation

5 Based on the report of doc. JUDr. Ing. Michal Radvan, Ph.D.

of the resources and funds related to these tasks. The increasing importance of processes and activities related to the privatisation of public tasks seems to be one of the answers to the indicated challenges in this field.

The next speaker was Professor Elena Chernikova, who raised a very interesting topic relating to the challenges and problems in the development of financial activities of state and municipal units within the Russian Federation. This subject turned out to be very interesting from the perspective of other Central and Eastern European countries, especially since in her speech the professor raised many interesting legal and comparative aspects. After this presentation, prof. Monika Augustyniak stayed in the field of comparative analysis and presented a paper about participatory budget in Poland and in France – the direction of changes. Professor especially mentioned several differences in the way that the participatory budget is executed in Poland and in France and suggested that it would be good if the Polish legislator benefits from the French regulation to make this special kind of budget be more civil than it actually is. The research studies referring to the Russian Federation Law were completed by the intermediary of the presentation prepared by the next speaker, Prof. Elene Kireeva. Professor Kireeva pointed out several problems of formation of municipal finances in the Russian Federation. It is crucial to underline that apart from the comparative aspects presented during this presentation, Prof. Kireeva was very often referring to the publications and conclusions of the previous International Baltic Conferences that shows the importance and topicality of the analysis and publications that were previously released by the organisers. Dr Rafal Kowalczyk ended the part of the session related to the doctrinal approach. He tried to determine the limits of the economic activity of local government units on the local market. The possible limits were analysed in reference to the judgment of the Supreme Administrative Court from 16. 5. 2006 and the hypothesis supposing that the category of collective needs of the community is constantly evolving and stimulating the actions undertaken by local government units.

Presentations delivered by the Regional Chamber of Audit representatives concluded the session. They applied to and solved in practice all the problems and challenges mentioned previously during the session. The first practical

point of view was related to the citizens' budget in local government units and was presented by Małgorzata Kopowicz and Alicja Śróbkowska. The second practical issue was specified by Roman Fandrejewski and Marian Kujawski and was related to strategic planning, long-term financial forecast, annual budget, financial and non-financial measures of achievements of local government units in the light of the report on the status of the municipalities. The session "Financial law of the local government units" was full of discussion related to the issues end challenges presented by the speakers, but it had to be ended by the moderator Dr Michał Mariański – who appreciated the scientific, comparative and practical level of all the presentations and suggested continuing the discussion also outside the conference panel and after the conference.[6]

A large number of conference participants from Russia, from many distant universities, enabled the organisation of a separate panel devoted to the problems of the financial law of the Russian Federation. The panel turned out to be a very successful undertaking for both interested conference participants and the panellists themselves. At our conference, they had the chance to meet to exchange many valuable comments and observations regarding financial law and its application in Russia. Panel "Financial Law of the Russian Federation" was moderated by Prof. Marina Sentsova. The financial and legal section of a conference was devoted to both theoretical, and practical issues of financial law. Tatyana Nikolaeva, the associate professor of the institute of public service and management, presented her report "Uncertain legal status of the Central bank in Russia." She made a comparative analysis of the foreign practice of the Central Bank's activity and pointed out that it belonged to state bodies and was independent. Roman Kirsanov, associate professor of the Dostoevsky Omsk State University, paid attention to the problem of financial and legal aspects of the organisation of the labour protection in Russia. Special attention was paid to the radical changes that are planned in the legislation on labour protection. Olga Popova, associate professor of the Immanuel Kant Baltic Federal University, spoke about the financing of the agro-industrial complex in Russia. She stressed that

6 Based on the report of Member of Association Henri Capitant des Amis de la Culture Juridique Française, Associate Professor at the Department of Financial Law at the Faculty of Law and Administration of the University of Warmia and Mazury in Olsztyn.

one of the ways to develop state funding of agriculture was to shift from the process form of financing to project financing. Yulia Tsaregradskaya, professor of financial law at the Kutafin Moscow State Law University, outlined the problem of online cash desks in the system of tax control, features of legal regulation. Irina Panina, assistant Professor of the Voronezh State University, highlighted the influence of changes in the legislation on Russia audit market highlighted. Artem Krivosheev, a postgraduate student of the Voronezh State University, spoke about the peculiarities of public finance management in the sphere of higher education in the Russian Federation.[7]

Prof. Mariusz Popławski moderated the panel "VAT – selected issues." Five speakers took part in this panel. In her speech "VAT fraud in French law. Selected issues", Prof. Mariola Lemonnier stressed that it is worth assessing implemented solutions regarding tax fraud in VAT, including judicial decisions in other countries. Therefore, France can be a very valuable comparative source for the assessment of legal solutions introduced in Poland. In the speech of prof. Witold Modzelewski's "Trends in the evolution of substantive tax law aimed at reducing VAT fraud", the issue of the VAT gap and the question as to the reasons for its significant reduction in Poland in recent years was raised. Referring to this issue, the clerk pointed out that the primary reason was the introduction of serious criminal sanctions penalising frauds in VAT refunds. Prof. Artur Mudrecki in his speech "Complex services in value added tax in the light of the jurisprudence of the Court of Justice of the European Union and the Supreme Administrative Court," mentioned the problem of the lack of a legal definition of the complex services concept, including tax, the solution of which should be sought in the jurisprudence of both abovementioned courts. In the speech of Vladimír Svitek, Perspective features of VAT digitising, the issue of the need to change tax law, primarily concerning VAT, was raised in order to adapt these regulations to the changing situation of entrepreneurs. This change applies to, among others, a steady increase in the number of activities related to conducting business activities that are carried out using the opportunities arising from the Internet. Professor Vladimír Týč, in the paper "Indirect taxes in EU law – recent developments after the crisis", pointed out the pros and cons of legal

7 Based on the report of Prof. dr Marina Valentinovna Sentsova, Voronezh State University.

solutions that can be introduced in the European Union in the near future in the field of tax on goods and services and concerning trade in goods between countries The European Union. A very lively discussion, which lasted about 45 minutes, started after the speakers' speeches. Apart from moderating this panel, the following spoke in the discussion: Prof. W. Modzelewski, Prof. L. Etel, Prof. D. Gajewski, Prof. A. Mudrecki, Dr J. Marczak. The discussion mainly concerned about the issues raised in the paper of Prof. Modzelewski. As part of the exchange of views, several issues were raised. On the one hand, a belief was expressed that the effectiveness of many tax law provisions cannot be assessed solely by the perspective of how often they are applied. This applies above all to provisions that are to perform a preventive function, preventing unwanted actions of taxpayers. On the other hand, it was argued that the role of criminal regulations penalising specific, improper taxpayers' activities could not be overestimated. Benefits that taxpayers can achieve because they violate the provisions of tax law may turn out to be more "appealing" than being aware of the criminal consequences that these entities may incur in certain situations.[8]

Prof. Rafał Dowgier moderated the panel "Financial law – selected issues" where six papers were presented. The speeches could be characterised by a great variety in terms of substance but inscribed in the broadly discussed topic of the conference. In the first paper entitled "Supervision over the activities of entities in tax capital groups. De lege lata and de lege ferenda conclusions" dr hab. Sebastian Skuza, prof. UW and Dr Robert Lizak presented underlying problems related to the subject matter. The postulates formulated by the speakers related to the need to change the current supervision system, including proposals of specific normative solutions, were particularly interesting. The next speech concerned issues related to the principle of balance between public and private financial interest in public procurement. Vitaly V. Kikavets presented these problems on the example of solutions in force in the Russian Federation. It should be emphasised, however, that the comments made in the paper were universal and they may contribute to a general discussion on the public procurement system. A particularly interesting paper was delivered by dr Andrzej Michór, bearing in mind legal disputes in Poland

8 Based on the report of dr hab. Mariusz Popławski, prof. UwB.

related to the borrowers' questioning loan agreements for which the Swiss currency is the appropriate currency. His subject was the issue of the substitutability of abusive provisions in credit agreements denominated and indexed to foreign currencies. The presentation presents possible options for resolving the situation in which the loan agreement contains prohibited clauses, with reference in this respect to the case-law of national courts and the CJEU. In the next speech, Tomasz Woźniak referred to the issue of progressive tax base erosion from international tax law in the context of the BEPS (Base Erosion and Profit Shifting) which is a project started by the OECD in 2013. The lecturer focused on analysing this project in the context of counteracting "artificial avoidance of establishment" and presented very interesting conclusions in this respect. The presentation of Dr Magdalena Mosionek-Schweda focused on the broadly understood issue of introducing pro-ecological solutions, in particular in the sphere of public finances. The panel ended with Mgr. Szymon Moś, who delivered a paper on "Non-clinical criteria in the procedure of evaluation of health care policy programs under public financing – systematic and financial aspects." After the speakers' presentations, the panel moderator held a lively discussion on the issues presented. As can be seen from the topics mentioned above, the speeches were characterised by far-reaching diversity. However, this does not change the fact that their scientific level was high, and the views expressed were not limited to a critical analysis of existing solutions, but also indicated the desired directions of changes in the law.[9]

During the 5th International Baltic Conference on Financial Law, the organisers met the demand of people interested in the conference but could not participate in the cruise. Therefore, they organised an on-line panel where participants could present their papers. If this form is adopted in the future, we will consider the possibility of full participation in the entire conference or at least part of it. Prof. Edward Juchniewicz took the difficult role of moderating this panel. The entire panel was devoted to tax issues presented on the example of legal regulations in Poland and Russia. A supplement to tax issues was the speech of Dr Tomasz Sowiński, who presented the problems of the social insurance system in Poland. Dr Sowiński presented his own opinion

9 Based on the report of dr hab. Rafal Dowgier, prof. UwB.

regarding the independence of the social security system from the state budget. Professor A. Dobaczewska gave a speech regarding the role of the European Commission decisions for implementation of state aid rules in taxes. Professor A. Dobaczewska tried to answer the question whether numerous EC decisions adopted or being (currently) under ECJ appeal procedure will change considerably the way the notion and range of state aid are understood, especially in taxation. Dr Dariusz Zając chose one of the most discussed topics related to taxes in Poland and gave us a lecture on the implementation of the exit tax to the Polish legal system. Dr Zając tried to confirm the hypothesis that implementation has been carried out correctly concerning European freedoms and made some de lege ferenda postulates. Professor Anna Kopina took one of the most complex topics in the field of international tax law, which is the problem of the beneficial owner of income. She presented the analysis of court decisions in Russia. Professor Zbigniew Ofiarski presented a paper entitled "Exemptions of port infrastructure from property tax in Poland". One of the aims of the speech was to present a comprehensive analysis of tax legislation, the case law and the achievements of the tax law doctrine, premises of and principles for exempting port infrastructure from property tax in Poland. Professor Małgorzata Ofiarska presented a paper entitled "Legal status of entrance fees to national parks and nature reserves located on the territory of the Republic of Poland". The main purpose of the paper was to analyse and assess the normative material and the achievements of the doctrine of law concerning such fees. As a result of the conducted research, it was shown that entrance fees to such special areas have a public law nature.[10]

Independent though coherent scientifically and substantively part of the 5th International Baltic Conference on Financial Law "The Financial Law towards Challenges of the XXI century" was the 1st International FLR Scientific Seminar. The seminar included three panels; two scientific and one organisational, and extraordinary meeting of the FLR Editorial Board, as well as a promotional part as part of the plenary session in Öland. The first panel "Financial law – general issues" was moderated by prof Anna Zalcewicz, and according to her report, it had the following course. As part of the moderated panel, three currents of consideration could be distinguished.

10 Based on the report of Dr Hab. Edward Juchniewicz, Prof. UG.

The first trend was related to the topic of public law receivables. Prof. dr hab. Jadwiga Glumińska-Pawlic (Counteracting the depletion of budget revenues – an attempt to assess new instruments) and dr hab. Wojciech Gonet (Responsibility for failure to collect public liabilities. Selected issues) delivered their speeches. Mrs prof. dr hab. Jadwiga Glumińska-Pawlic has assessed the instruments for preventing the reduction of budgetary revenues, in particular in the form of reverse charge mechanism, uniform control file, clearinghouse ICT system (STIR), additional tax obligations (sanctions resulting from the provision of Article 112b of the Act), the "fuel package "," Energy package ", split payment. Dr hab. Wojciech Gonet in his speech considered, among other things, whether local government units and the State Treasury have legal regulations enabling effective recovery of small individual due monetary claims. The speaker showed that SP and JST may lose civil law income due to the lack of appropriate regulations enabling the recovery of small amounts due. He pointed to the need to extend the limitation period for civil law liabilities of SP and local government units and the legitimacy of punishing those responsible for failure to pay JST and SP's due claims with financial penalties specified in the Act on liability for violation of public finance discipline.

The second part of the discussion was related to public procurement. Dr. Anna Wójtowicz-Dawid (Public sector as a smart client and effective public procurement) and Dr. Maciej Bendorf-Bundorf presented their views (Social clauses in public procurement procedures in the light of efficiency of public expenditure). The issues of efficiency were assessed from the cost-efficiency of spending and the impact of social clauses on public procurement point of view, as well as the very understanding of the concept of "efficiency". Doctor Maciej Bendorf-Bundorf drew attention to the fact that, in principle, the most important in public procurement is the benefit determined based on economic calculation, taking into account the quality and functionality of the products purchased. However, the effectiveness of public expenditure must be considered in a broader context than just the savings of a specific contracting authority and the cost of a specific public contract. This is due to the fact that modern public procurement, including

social clauses, is designed to perform not only the function of purchasing goods and services for the public sector but also specific social functions.

The third trend concerned financial market law. The following participants spoke in the discussion: Dr Rafał Mroczkowski (Financial system stability in holistic terms. Contribution to the discussion) and Magister Maciej Mikliński (Competences of the Polish financial supervisory authorities in the light of inappropriate clauses in the bank's consumer contracts). Dr Rafał Mroczkowski emphasised that the stability of the financial system should be considered in a broad context. He pointed out that the current legal solutions are not optimal. An example is the regulation of macro-prudential supervision. In this context, he critically assessed, inter alia, the assignment to the tasks of the NBP of actions for the stability of the financial system, as it would be more appropriate to indicate that such actions should be the NBP's goal. The speaker also raised the problem of insufficient cooperation between NBP, BFG and KNF within the security network. Mr Maciej Mikliński presented the competence problems of the Polish financial supervisory authorities regarding abusive clauses used in the practice of banks. The speech contained a synthetic presentation of the reasons for treating banks as institutions of public trust and contradicting this image of the fact that banks used hundreds of abusive clauses in consumer contracts. Some of these clauses, such as clauses enabling banks to freely change the content of the legal relationship, free change in the interest rate on loans, or recalculating claims at the exchange rate freely set by the bank, pose severe systemic risks. They cause effects on several levels. In civil law terms, abusive provisions do not bind the consumer and, as a consequence, create a gap that is very difficult to fill without the consent of the consumer. In addition, such cases may cause a reaction of the President of the Office of Competition and Consumer Protection imposing a fine up to 10 % of annual turnover for the use of prohibited contractual provisions. Besides, the scale of irregularities may cause reactions from politicians imposing additional restrictions on banking activities. The issue of counteracting such risks that may destabilise the market lies within the competence of financial supervision, including the PFSA has a statutory obligation to ensure compliance of granted loans and borrowings with applicable regulations (Article 133(2)(3) PrBank).

The scale of banks' problems caused by the use of abusive clauses and the scale of KNF's omissions is currently difficult to estimate. In the absence of comprehensive proposals to solve these problems, interested consumers are waiting for courts to develop case-law and then the full scale of the problem may be revealed.[11]

During the 2nd panel of the FLR seminar "Financial law and the financial market – selected issues" whose moderator was Prof. Dominik Gajewski, lectures were delivered by seven participants. Prof. Witold Srokosz presented law and innovations in the financial market. In the next lecture, Prof. Patrycja Zawadzka talked about derivatives in the public finance sector. Prof. Anna Zalcewicz presented the issues of financial technology and service provision in the context of new challenges in the field of consumer protection in financial services. Prof. Anna Jurkowska-Zeidler presented challenges for financial market regulation a decade after the global crisis. Dr Cyman Damian presented a lecture about redefining the concept of a consumer in the financial market, and Dr Michal Janovec told us how not to abuse the market. In a recent paper, Dr Pawel Szczesniak presented issues of a legal relationship between the authorities of the financial security network. The panel ended with a discussion of participants.

The conference ended with a plenary summary session moderated by Prof. Witold Modzelewski, during which the moderators presented the content and course of all sessions and panels. After the last session, there was a discussion of all participants of the 5th International Conference on Financial and the 1st International FLR Scientific Seminar, summarising the entire conference and 5th edition of the scientific project "Financial Law towards Challenges of the XXI century".

All participants of the 5th International Baltic Conference on Financial Law expressed their appreciation for the scientific and organisational level of the conference and their intention to participate in the 6th edition due to take place in 2021.

Tomasz Sowiński, Ph.D.

11 Based on the report of dr hab. Anna Zalcewicz, profesor uczelni (PW).

THE FINANCIAL LAW TOWARDS CHALLENGES OF THE XXI CENTURY

Assoc. Prof. JUDr. Petr Mrkývka, Ph.D., Prof. zw. dr hab. Jolanta Gliniecka, Ing. Eva Tomášková, Ph.D., Dr Hab. Edward Juchniewicz, Prof. UG., Dr Tomasz Sowiński, Ph.D., Assoc. Prof. JUDr. Ing. Michal Radvan, Ph.D. (eds.)

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