Tax administration practise and Legal protection[1]

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1. Introduction

May a taxpayer rely on the opinion of the tax inspector with respect to the tax consequences of a certain envisaged transition, also if this opinion appears not to be in line with the law? Should the judge honour the expectations raised by the opinion, or should he apply the law? This contribution deals with these kind of questions.

At first sight, from the viewpoint of the doctrine of the separation of powers as a rigid separation of powers, tax administration practise does not seem to be a very interesting issue. Indeed, in this rigid view, the administration seems to be stuck between the power of the legislator and the power of the judiciary. On the one hand, the legislator provides for general rules and the administration should 'only' apply these rules in concrete cases. On the other hand, the judiciary reviews – in case of a conflict – whether this application is correct. Especially in tax law there seems to be barely room for an independent administration practise, for the principle of legality is of great importance in tax law: no taxation without a legislative basis. The principle of legality in the tax context also implies, strictly, that the tax administration must apply the legislation, and that it therefore has no competence to deviate from the legislation in favour of the taxpayers.

However, the Netherlands tax practise shows the administration's position in the field of tax law is far more important than the position described above. First, nowadays in the Netherlands constitutional context, there is no

[1] Parts of this chapter have also been discussed in Richard Happé and Melvin Pauwels, `Balancing of powers in Dutch tax law: general lines and recent developments', in: Judith Freedman en Chris Evans (ed.), *Tax Discretion and the Rule of Law*, forthcoming (IBFD), 2011.

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rigid application of the doctrine of the separation of powers. Especially the "two hats" of the State Secretary of Finance are of importance. The State Secretary is head of the Netherlands tax administration and is politically accountable for the performance of the tax administration to Parliament. In this way, the State Secretary is part of the administration. Besides, the State Secretary of Finance is "co-legislator". In the Netherlands, in general, the enactment of an Act of Parliament is not a task of Parliament alone, but it is a task of Parliament and government together and the State Secretary of Finance – like other State Secretaries – is part of the government. Both government and Parliament may initiate legislation by presenting a Bill. However, on most occasions, it is the government that presents Bills. With respect to taxation this means that it is the State Secretary of Finance who introduces tax Bills into Parliament. Secondly, also *de facto* the powers between the legislator and the administration are not rigidly separated. The tax administration has influence on the contents of the legislation. One factor is the just described central role of the State Secretary of Finance in the establishment of tax legislation. The second factor is that it is generally noted on tax literature that it appears to be difficult for the Parliament to provide an effective counterbalance in the legislative process to the power of the State Secretary of Finance. We dealt with these two issues – the "two hats" of the State Secretary and the tax administration's influence on the legislation – in another publication.[3]

In this chapter, we deal with another subject that shows that in the Netherlands there is no rigid application of the notion of separation of powers. Here, we do not deal with the tax administration's influence *on the legislation*, but we focus on another aspect: the discretion of the tax administration when *applying* the tax legislation. This discretion raises several interesting issues, especially with respect to the legal protection of taxpayers. That is a central issue in this chapter: the consequences of tax administration's discretionary power for the legal protection of taxpayers.

[3] Happé/Pauwels 2011. See also, *in extenso*, Hans Gribnau, "Separation of powers in taxation: The quest for balance in the Netherlands", in Ana Paula Dourado (ed.), *Separation of Powers in Tax Law*, European Association of Tax Law Professors International Tax Series vol. 7, Amsterdam: IBFD, 2010.

In that respect we deal with several topics. First, we provide a short overview with respect to the tax administration's discretion when applying the tax law in the Netherlands. Then, in section 3, we discuss whether the tax administration has such discretion. In that respect, we analyse the concepts like '*contra legem*', and '*praeter legem*' and '*inter jus'*. Subsequently, in section 4, we deal with some general aspects of the counterbalancing by the judiciary in response to the discretion of the tax administration for the purpose of the legal protection of taxpayers. In section 5, we first note that the exercise of discretionary power by the administration– sometimes beyond the boundaries of the legislation in the strict sense – could in principle cause problems, from the view of both the rule of law and the legal protection of taxpayers. Secondly, we analyse how the judiciary provided for legal protection based on the so-called "principles of proper administration behaviour." In that regard, we introduce the concept of "priority rules" to denominate the rules that the Supreme Court provided when balancing the principle of legality against a principle of proper administration behaviour. In section 6, we discuss in more detail priority rules with respect to principles of proper administration behaviour that are the most important in tax practise, viz. the principle of equality and the principle of legitimate expectations. The chapter ends with some final observations.

2. Tax administration's discretion in the Netherlands; a short overview

2.1. Introduction

In strictly formal terms, the Netherlands tax administration has no discretionary power when applying the tax legislation (besides some minor exceptions). Tax statutes usually do not grant discretion to the administration. The tax burden of a taxpayer is a "logical" consequence of the application of the tax rules to the facts concerned. This relates to the principle of legality. This principle with regard to taxes is laid down in article 104 of the Constitution. This provision reads as follows: "State taxes are imposed by force of a statute." On the one hand this implies that no tax may be imposed by the tax administration if there is no basis for it in a tax

statute.[4] Moreover, related, if there is a basis in a statute for the taxation concerned, the level of taxation is limited to the amount of taxation that can be derived from the statute concerned. On the other hand, the principle of legality – viz. the principle that the statute should be applied – also implies that the tax administration should not deviate from the statute in favour of a taxpayer. So, the tax inspector should not impose too much tax but neither too little; he should impose tax to the correct level. Obviously, this also relates to the principle of equality.

Notwithstanding that, strict formally, the Netherlands tax administration has no discretionary power when applying the tax legislation, in practise and traditionally, the tax administration does have discretionary power. We note that Supreme Court has confirmed that the Netherlands tax administration indeed has some competence in this respect; see section 3.2.

In this section we shortly discuss some examples of the exercise of tax discretion by the tax administration. First, we deal with rules provided by the tax administration, amongst others "policy rules". Then, an "opinion" by the tax inspector and a "settlement agreement" between a taxpayer and a tax inspector are discussed. Subsequently, we shortly introduce the phenomenon of "enforcement covenants". Finally, a relatively new provision in the General Tax Act is discussed that involves more procedural room for the tax administration when applying the tax law.

2.2. Rules provided by the administration

Not only the legislator provides tax rules. Also the administration sometimes makes rules. Two types of rule-making by the administration should be distinguished.

First, the rule-making may have an explicit legal basis. This is the case if the legislator gives the administration the authority to make rules in a delegation provision. If based on delegation, the judiciary in principle must respect these rules made by the administration.

[4] Compare Supreme Court 8 October 1993, no. 15101, BNB 1994/19 and Supreme Court 8 May 1998, no. 16553, NJ 1998/890.

Secondly, rule-making by the tax administration may happen by means of so-called "policy rules". Basically, two types of policy rules should be distinguished.

The first type is the so-called "interpretative policy rule". By means of such a published rule the tax administration makes known what, in its view, is the correct interpretation of a certain statute. Such a rule offers taxpayers certainty about how the administration will apply the statute concerned. Obviously, in the end, the judiciary decides what the correct interpretation of that statute is. However, until that time the interpretative policy rule has a major influence on tax practice. Indeed, taxpayers who do not wish to go to court will follow the interpretative policy rule.

The second type is the so-called "approving policy rule". In the case of such a rule, the tax administration makes known that it approves – in favour of taxpayers – a certain application of the tax legislation in a specific situation even though this application deviates from the strict wording of the statute concerned. So, here, the administration deliberately deviates from the strict application of the rule provided by the legislator.

Note that there is a difference in character between both types of policy rules.[5] An "interpretative policy rule" provides an opinion of the tax administration that is intended to be *intra legem*. To the contrast, in case of an "approving policy rule" the tax administration deliberately deviates from the strict wording of the statute concerned, and such a policy rule could therefore be considered to be *contra legem*. Note however, as we discuss in section 3.3, that a further distinction is needed. It will appear that such a *contra legem* rule might be not really *contra legem* but instead should be qualified as *praeter legem*.

In general, these policy rules, both the interpretative and approving types, are considered of great importance by taxpayers. They provide for certainty, give feasible solutions for complications in the law or offer more appropriate applications than is possible according to the strict wording of the statute. Especially in the domain of businesses, no taxpayer can afford to ignore these rules. It should be noted that this type of influence of the

[5] Richard Happé, *Drie beginselen van fiscale rechtsbescherming* (Phd-thesis), Deventer: Kluwer, 1996, pp. 27-28.

tax administration on the application of the tax law regards the contents, unlike – in principle – the types discussed in section 2.4 and 2.5.

2.3. Opinion and settlement agreement

The previous section concerned *general* rules of the tax administration, more in particular the State Secretary of Finance. Traditionally, the tax administration may also provide certainty, even in advance, to an individual taxpayer with respect to a specific situation. This usually happens at the implementation level, so at the level of the tax inspector. Nonetheless, the tax inspector may seek contact with the policy makers at the Ministry of Finance if the case at hand has general aspects that could also be of relevance for other taxpayers.

The traditional possibility for taxpayers, especially companies, to have contact with the tax inspector and to obtain certainty in advance relates to the famous so-called "ruling practise" for companies.[6] This Netherlands "ruling practise" was placed on the black list by the Primarolo-group.[7] Further to this listing, the "ruling practise" has been converted into a practise for ATR's (advance tax rulings) and APA's (advance pricing agreements).[8] Main difference with the "ruling practise" is that an ATR or an APA is concluded based on an assessment of the individual circumstances ('tailor-made'), while the "ruling practise" was based on relatively fixed standards or rules ('ready-to-wear'), for example standard 'spreads' with respect to financing activities.

Generally, the tax authorities could provide certainty in advance with respect to the tax consequences of a specific case in two ways. First, upon request of a taxpayer, the tax inspector could provide his opinion with respect to the tax consequences of a certain transaction. Note that such an "opinion"[9] is unilateral. So, the taxpayer is not bound to the opinion. If the

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[6] See amongst others on this subject C. Romano, *Advance tax rulings and principles of law; Towards a European tax rulings system?*, Amsterdam: IBFD, 2002.

[7] See e.g. Maarten J. Ellis, 'The Code of Conduct in 2000: Cracking the Code or Coating the Crack?', *European Taxation* 2000, pp. 414-416.

[8] See for example Hans Pijl and Wobke Hählen, The New Advance Pricing Agreement and Advance Tax Ruling Practice in the Netherlands, *Bulletin for International Taxation* 2001, pp. 614-629.

[9] Netherlands case law and literature also discerns the "promise" (*toezegging*), which could be considered as a species of an "opinion" (*standpuntbepaling*). Another example of an

taxpayer at a later stage has the view that the tax consequences are different, the taxpayer is still allowed to take that position and may start legal proceedings (if the tax administration disagrees with that position). By contrast, as we discuss in section 5.4 and 6.2, the tax administration is in principle bound to such opinion, even if the opinion is not in line with the correct interpretation of the statute concerned.

Secondly, if the application of a statute in a specific case is unclear, a taxpayer may enter into an agreement with the tax inspector with respect to the tax implications. Such an agreement is considered an agreement under civil law, more specific a settlement agreement (*vaststellingsovereenkomst*) in the sense of article 7:900 of the Netherlands Civil Code. This implies that, unlike in case of an opinion of the tax inspector, not only the tax inspector but also the taxpayer involved is in principle bound to this type of certainty in advance, as it concerns a bilateral agreement.[10] Obviously, it could be that, after the conclusion of the agreement, the taxpayer and the tax inspector disagree about whether or not a certain issue falls within the scope of the settlement agreement. Case law shows that there are sometimes legal proceedings in which the dispute concerns the scope of a settlement agreement.

2.4. The phenomenon of "enforcement covenants"

As from 2005, there is a fundamental change in method by the Netherlands tax administration to promote compliance by taxpayers. The tax administration has started to enter into "enforcement covenants" with taxpayers.[11] In the initial years, such covenants were concluded with multinationals operating in the Netherlands. The approach is now applied in a wider range. Covenants are also concluded with national enterprises, including medium-sized enterprises. Furthermore, there is an indirect variant of the approach, in which the tax administration concludes enforcement covenants with tax intermediaries, in particular tax advisory

"opinion" is the "declaration of agreement" (*akkoordverklaring*). See Happé 1996, pp. 184-201 in this regard.

[10] For example Supreme Court 21 February 2001, no. 35551, BNB 2001/149 and the opinion of the Advocate-General Van Kalmthout for this decision.

[11] See, with respect to this development, Richard Happé, "Multinationals, Enforcement Covenants and Fair Share", *Intertax* 2007, pp. 537-547.

companies that assist taxpayers with filing their tax returns. It seems that more than half of tax intermediaries have such a covenant at the moment.[12] This new method of concluding enforcement covenants with taxpayers can be considered "an unconventional, almost revolutionary method of exerting a positive effect on and supporting (…) compliance, entailing horizontal supervision embedded in a vertical supervision framework" that is based on "mutual trust".[13] One of the core elements of horizontal supervision is that the tax administration relies on the auditing activities of the businesses or their intermediaries. An element of an "enforcement covenant" is often that the tax administration conducts a dialogue with taxpayers and makes arrangements in advance about the tax consequences of envisaged transactions. In this context, one of the fundamental changes of this method is that the supervision is shifted in two ways: (a) from almost fully vertical to largely horizontal, and (b) from almost fully ex post to largely ex ante. We note that this approach of concluding "enforcement covenants" is new, but it fits – as a new element – in the tradition that the Netherlands tax administration exercises discretionary power when implementing tax law.[14]

There is no question that this new approach has positive effects, for the tax administration as well as for taxpayers. One of the main advantages for taxpayers is that they have certainty with respect to their tax debt and the tax consequences of their transactions at an earlier stage, even in advance of the transactions. It should also be noted that for companies it is increasingly important to have an enforcement covenant with the tax administration for reasons other than taxation. It is important for both their annual report and their reputation. It is regarded as a sign of "good corporate governance" to have an enforcement covenant.

Besides the positive effects, this new approach may have, however, from the perspective of the balancing of powers, an interesting side effect. This possible effect is that the judiciary is partly "sidelined", for taxpayers may be reluctant to go to court, in order not to put their relationship with the tax

[12] Only when the taxpayer agrees in turn with the covenant of his tax intermediary, the covenant is also binding him.
[13] Happé 2007, p. 537.
[14] Happé 2007, p. 541.

administration "on the line". In that sense there is a shift of power from the judiciary to the administration. We have elaborated on this subject in another publication.[15]

2.5. Increased procedural room for tax administration

Besides, there has been a legislative development leading to increased room for the tax administration when applying the law. This development does not regard tax with respect to the contents but regards a procedural discretion. It concerns the relatively recent introduction of article 64 of the General Tax Act as per January 1, 2008.[16] This introduction should be understood in the context of the following background.

In some situations it was and is more efficient for the tax administration to levy taxes in a way that is not fully in line with the formal procedures laid down in the tax statutes. An example concerns the situation in which a tax audit shows that a taxpayer should pay additional tax over a couple of tax years. Formally, the tax inspector should impose an additional tax assessment for each tax year involved. However, in practise, the tax inspector and the taxpayer involved may agree that only one tax assessment for one of the years is issued for the total amount of tax due over the years involved. Another example is the situation in which it appears (e.g. from a tax audit by the administration) that some companies, all belonging to the same group, have underpaid wage taxes. It is then more efficient for the tax administration to impose just one additional assessment on one of the group companies for the total amount of tax than to impose additional assessments on each of the companies. However, the imposition of just one additional assessment on one of the group companies for the total group amount of tax due strictly speaking is not in line with the tax law: a taxpayer can only be assessed for his own tax. The judiciary has allowed some discretion to the administration with respect to an efficient application of the law. However, if a particular "efficient" method has deviated too much from the correct procedure according to the tax Acts, the

[15] Happé/Pauwels 2011.
[16] Act of 20 December 2007, State Gazette 2007, 563, article XVA.

judiciary has not allowed such a method because of the legal protection of the taxpayer involved.[17]

This review by the judiciary is now limited by article 64 of the General Tax Act. This provision stipulates that "for the advancement of an efficient formalization of a tax debt (…), the inspector may deviate from [the method] which the tax Acts stipulate otherwise". A requirement is that the taxpayer should agree with the method of formalization. So, we observe that the administration – the tax inspector – is granted more discretion, not with respect to the amount of tax levied, but with respect to the method of formalization. Thus, the judiciary should respect the method of the tax inspector, even where the inspector deviates from the method that the tax Acts stipulate. Paradoxically, such non-compliance with the tax Acts by the tax inspector is based on a tax Act (article 64 of the General Tax Act). So, the non-compliance has the explicit consent of the legislator and in that way has the character of compliance again.

2.6. Conclusion

The above overview shows that the statement that the tax administration 'only' applies the tax law and has no discretion, has no factual basis in Netherlands tax practise. Instead, the tax administration has great influence on the application of the tax law. The above-mentioned four types can be distinguished in two categories. The last two types have in common that they concern procedural discretion of the tax administration, i.e. discretion with respect to the method of formalization of the tax due. Obviously, both types may also influence the taxation with respect to the contents, but that is not the general feature of these types. Taking into account the subject of this contribution, we do not deal with these types in the remainder of this contribution.[18] In the remainder we focus on the other (first) two types. These types concern the discretion of the tax administration with respect to the contents. So, this discretion has influence on the actual tax that is due.

[17] Supreme Court 3 June 1981, no. 20281, BNB 1981/230.
[18] See Happé/Pauwels 2011.

3. Discretionary power of the tax administration inside the boundaries of the law

3.1. Introduction

In the next section, we show how the judiciary has responded to the above-described discretion of the tax administration. First however, in this section, we note that the Supreme Court has confirmed that the tax administration has indeed some discretionary power when applying the tax law. We discuss a landmark judgement of the Supreme Court in this respect. Then, we argue that an application by the tax administration that deviates from the strict wording of the statute should be qualified as praeter legem instead of contra legem, where that application is intra jus.

3.2. Landmark judgement: confirmation of discretion of the tax administration

In a landmark judgement in 1978, the Supreme Court gave its opinion about the issue whether or not the tax administration has some discretionary power when applying the tax law. This consideration points out that according to the Supreme Court the Netherlands tax administration indeed could have competence to provide for additional (policy) rules and thus has insofar some discretionary power. The tax administration has competence to provide for additional rules – we quote the Supreme Court – in cases

"hat have not been foreseen by the legislature or cases that are not specifically regulated in the legislation – for example for the purpose of uniform interpretation and application of the tax legislation, for the advancement of the practical feasibility of the tax legislation, in order to do more justice to the principle underlying the legislation than does the strict wording of the legislation, or to meet substantial unfairness."[19]

Note that in Netherlands literature it was already stated prior to this judgement that the tax administration has the competence to deviate from the strict application of the tax statutes in favour of taxpayers.[20]

[19] Supreme Court 12 April 1978, no. 18 452, BNB 1978/135.
[20] See Happé 1996, p. 33, with further references.

Interestingly, this landmark judgement not only confirms that the tax administration has indeed competence to provide additional rules in certain cases. Just because the judgement confirms this competence of the tax administration, the judiciary also achieves the result that it can offer legal protection to taxpayers. As we discuss in section 5 and 6, the administration is bound by its own rules.

3.3. *Contra legem* vs. *praeter legem*

As mentioned above (section 2.2), an "approving policy rule" could be regarded *contra legem*, based on the idea that the policy rule provides an application of the tax law in deviation of the strict wording of the statute concerned. The above-discussed landmark case of 1978 however indicates that the tax administration indeed has the competence to provide additional (approving) policy rules. This implies for two reasons that the qualification "contra legem" is not adequate in all cases.

The first reason is a formal, procedural reason. It contains that where there is competence to provide rules, the rule that is provided within the scope of that competence cannot be regarded as *contra legem*.

The second reason is a substantial reason. In that respect, it is important to have a closer look at the cases to which the Supreme Court refers where it mentions that the tax administration has the competence to provide policy rules. These cases concern "cases that have not been foreseen by the legislature or cases that are not specifically regulated in the legislation." In our view, the additional rule-making by the tax administration in such cases cannot not be considered genuinely *contra legem*. In fact, this rule-making happens because the legislation has shortcomings. For example, the legislation might be "underinclusive" (the case at hand does not fall within the scope of the statute concerned, while it should do so taking into account the purpose of that statute) or "overinclusive" (the case at hand falls within the scope of the statute concerned, while that should not be the case taking into account the purpose of that statute).[21] In other words, in such cases, the rule-making happens with the purpose to do justice to the peculiarities

[21] See for the concepts of "underinclusiveness" and "overinclusiveness" Joseph Tussman and Jacobus tenBroek, 'The Equal Protection of the Law', California Law Review, 1949, Vol. 37:341 and, recently, for example Gribnau 2010, par. 2.9.2.3.

of the case. Note in this respect also the examples that the Supreme Court mentions: "for the purpose of uniform interpretation and application of the tax legislation, for the advancement of the practical feasibility of the tax legislation, in order to do more justice to the principle underlying the legislation than does the strict wording of the legislation, or to meet substantial unfairness." Taking into account that this rule-making happens with the purpose to do justice, it is appropriate to say that such a rule is inside the law, *intra jus*. This also implies that, in our view, it is not appropriate to qualify the policy rule as genuinely *contra legem*, notwithstanding that the rule might not be in line with the strict wording of the statute concerned. Instead, the policy rule should be qualified as *praeter legem*.[22]

Concluding, an 'approving policy rule" that is strictly speaking *contra legem* should nevertheless be considered *praeter legem* if it is *intra jus*.

It should be noted that an approving policy rule cannot be qualified *by definition* as *praeter legem* and *intra jus*. Such a policy rule can only be considered so if the rule is introduced in line with the goal that the legislator has in mind with the statute concerned and respects the principle underlying that statute. However, if for example the tax administration introduces the policy rule for the purpose of its own economical or social considerations, the line between intra jus and extra jus has been crossed. Then, the policy rule *contra legem* cannot be qualified as *praeter legem*, but should be considered genuinely *contra legem*.

The above applies not only to policy rules of the tax administration but also – mutatis mutandis – to other ways the tax administration, including the individual tax inspector, uses its discretion. For example, the situation of an "opinion" of the tax inspector, discussed in section 2.3. Usually, the tax inspector has the intention that his opinion is in line with the correct interpretation of the statute concerned. However, in certain situations, the tax inspector may deliberately deviate from the strict wording of the statute. If this happens with the purpose to do more justice to the principle underlying the statute than the strict wording of the legislation the opinion could be qualified as "praeter legem".

[22] Cf. Happé 1996, pp. 37-39.

4. Legal protection of taxpayers by the judiciary; some general aspects

4.1. Introduction

In section 2, we have shown that the tax administration has important influence on the application of the tax law with respect to the contents. For example, the tax administration provides rules, and the tax administration may grant certainty about the consequences of an (envisaged) action by providing an opinion or by entering into a settlement agreement. As we show, interestingly, the judiciary has created "counterbalance" in response to this power of the administration. We deal with this response in two sections. In this section, we discuss some general aspects, especially with respect to the rule-making of the tax administration. In the next section, we discuss the fundamental approach of the judiciary to ensure the legal protection of taxpayers. This approach is based on the so-called principles of proper administration behaviour.

In section 2.2 we have shown that the tax administration makes rules. Here, we discuss that the judiciary has developed several mechanisms to counterbalance the administration's power. These mechanisms are aimed at securing the legal protection of taxpayers. We recall that a distinction can be made between the administration's rules that have an explicit legal basis in a delegation provision, and policy rules.

4.2. Administration's rules covered by a delegation provision and the legal protection by judiciary

If rules of the administration – usually rules of the Minister of Finance or the State Secretary of Finance – are based on a delegation provision in an Act of Parliament, the rules in principle count as law. So, the judiciary should in principle respect these rules and apply these rules in the same way Acts of Parliament are applied. There are however limits to the rule-making power of the administration. First of all, the judiciary verifies whether or not the rule concerned exceeds the boundaries set by the delegation provision. Usually, a delegation provision stipulates the subject on which, and the purpose for which, the administration may make rules. If the judiciary has the opinion that the rule concerned exceeds the boundaries set by the

delegation provision, the rule will be declared insofar invalid. Secondly, although rules of the administration in principle count as law, they do not have the same legal status as an Act of Parliament. Importantly, article 120 of the Constitution (which involves the rule that the judiciary may not test Acts of Parliament for compatibility with the Constitution or 'unwritten' principles of law) is not applicable to such rules. The judiciary is allowed to examine whether such rules are in line with the Constitution and legal principles. However, obviously, this examination may not result in an implicit testing of the contents of the Act of Parliament that provides for delegation (as this would be a de facto infringement of the aforementioned constitutional provision).

4.3. Other administration's policy rules and the legal protection by judiciary

As regards policy rules of the administration, the judiciary provides for substantial counterbalance to the administration. As mentioned in section 2.2, a distinction could be made between an "interpretative policy rule" and an "approving policy rule".

As concerns the first category, it should first be emphasised that the judiciary is not bound by such a rule. The power of the judiciary to interpret the statute concerned is not influenced by the interpretation laid down in the interpretative policy rule. So, although it cannot be denied that interpretative policy rules have influence in legal practice (as taxpayers will often adopt the interpretation of these rules), in the end, the "rule of law" in principle supersedes them.

Where the court has established the correct interpretation of the statute concerned, in general there are three possibilities. The interpretation put forward in the interpretative policy rule (1) appears to be the correct interpretation, (2) appears to be less favourable than the correct interpretation and (3) appears to be more favourable than the correct interpretation. In the second situation, the court provides legal protection by applying the statute according to its correct interpretation. So, the principle of legality then serves legal protection. In the reversed situation, the third situation, the court is in principle still not bound to the policy rule's

interpretation. However, then an issue of legal protection of taxpayers arises. After all, taxpayers may have relied on the "interpretative policy rule" of the tax administration. Should the courts honour these expectations, or should the courts apply the legislation? Here, the principle of legality collides with the principle of legal certainty, more in particular legitimate expectations.

The same issue arises with respect to "approving policy rules". Should the courts apply these rules, setting aside the legislation?

We deal with this issue in more detail in section 5 and 6 below, for this issue relates to the more general issue of how the judiciary has managed to provide for counterbalance, serving the rule of law and the legal protection of taxpayers, in response to the discretionary power that the Netherlands tax administration traditionally has exercised. At this moment, we only mention the result, namely that the courts do protect taxpayers' legitimate expectations based on the policy rule and thus grant the taxpayers a tax treatment that is in line with the policy rule.

5. Legal protection; principles of proper administration behaviour and priority rules

5.1. Introduction

We have noted that the tax administration has important influence on the application of the tax law. We have mentioned examples such as the "approving policy rules" and the possibility that the tax administration declares – often upon request of a taxpayer – the tax consequences of a particular transaction. In this section we first show that this important influence of the tax administration could in principle cause problems, from the view of the legal protection of taxpayers. We then analyse how the Netherlands judiciary has found a solution in the principles of proper administration behaviour. In this respect we refer to the concept of "priority rules" that has been introduced in the Netherlands literature.

We note that, in this section, we do not further expand on the legal protection in case a settlement agreement (*vaststellingsovereenkomst*) has been concluded between a taxpayer and a tax inspector (see section 2.3). In short, the legal protection for a taxpayer in that situation is that the tax

inspector is in principle bound to such an agreement – being a civil law agreement –, also if the tax consequences agreed on are not in line with the statute concerned.[23] Note that, on the other hand, also the taxpayer is in principle bound to the agreement, even if it appears that the tax due according to the agreement is more than the tax that would be due according to the statutes concerned.

5.2. Sketch of a dilemma

Due to the separation of powers, there is to a certain extent a safeguard against arbitrariness on the part of the administration. In the case of a conflict, the judiciary verifies whether the administration applied the legislation correctly. The central element in this respect is the legislation.

However, this basic approach is not fully adequate in the situation in which the administration has an important influence on how the tax legislation is applied. Suppose that a published policy rule of the tax administration is more favourable than the legislation. What should the court decide if a tax inspector imposes an assessment in accordance with the (less favourable) legislation and deviates from the policy rule? Likewise, suppose that a tax inspector declares to a taxpayer in advance the tax consequences of a particular proposed transaction. What should the court decide if at a later stage, on the occasion of raising the assessment, the tax inspector deviates from his earlier opinion, on the ground that the legislation prescribes other tax consequences than those he previously declared? If the legislation was the only criterion on which the judiciary was to judge the administration, the court should accept the assessment in both situations. Obviously, then, the rule of law and its goal of preventing arbitrariness would be at stake, as the tax administration would be allowed to arbitrarily deviate from earlier positions on which taxpayers relied. The principle of legal certainty, viz. honouring legitimate expectations, would be infringed. Furthermore, in the example of the policy rule, the principle of equality could be at stake in a situation where the tax administration might apply the favourable policy rule to other taxpayers.

[23] The same legal protection is provided in case of an 'interpretative policy rule' or 'opinion' that appears to deviate from the correct application of the statute concerned; see section 5.4 and 6.2.

5.3. Breakthrough judgments

Section 5.2 shows that, from the viewpoint of legal protection of taxpayers, it is not sufficient for the legislation to be the only criterion on which to judge the administration's decisions. Nonetheless, many years, until some landmark cases in 1978, the Netherlands judiciary held that the principle of legality superseded. Complaints about the behaviour of the tax administration had to be addressed to the State Secretary of Finance.

In 1978, the Supreme Court ruled several cases on the same date. In these tax cases the Supreme Court ruled that, under circumstances, the principle of legality could be outweighed by "principles of proper administration behaviour". The Supreme Court considered:

"that the task of the tax justice when judging the lawfulness of a tax assessment is not limited to the question whether the Inspector has stayed within the boundaries set by the legislation, but the justice's intervention is also required if the manner on which the Inspector has executed his competences is otherwise contrary to the law, for he has acted inconsistent with principles of proper administration behaviour that should be respected;

that under circumstances strict application of the legislation, as from which the tax due directly results, may infringe one or more principles of proper administration behaviour to that extent that this application should be refrained;

that, in general, the question under which circumstance the latter occurs should be answered case-by-case by balancing the principle that the legislation should be applied against the principles of proper administration behaviour that are involved."[24]

Netherlands literature calls these landmark cases as "breakthrough judgments". These judgments concerned the principle of legitimate expectations. However, the considerations of the Supreme Court have a general character and thus indicate that they are also relevant for other principles of proper administration behaviour. Within a short term, the Supreme Court also confirmed this with respect to principle of equality.[25] Subsequent case law shows that also other principles of proper

[24] Supreme Court 12 April 1978, no. 18452, BNB 1978/135.
[25] Supreme Court 6 June 1979, no. 19290, BNB 1979/211.

administration behaviour could involve that the tax authorities should refrain from the strict application of the legislation. An example is the principle of due carefulness.[26] Nevertheless, the principle of legitimate expectations and the principle of equality are the most important principles of proper administration behaviour in tax practise. In judicial proceedings, taxpayers often refer to these principles. Therefore, in the next sections, we mainly focus on the principle of legitimate expectations and the principle of equality (both as principles of proper administration behaviour[27]).

5.4. Applying principles of proper administration behaviour by the judiciary: the method of priority rules

The breakthrough judgments indicate that, under circumstances, a principle of proper administration behaviour could involve that the tax authorities should deviate from the correct application of the legislation. Moreover they show that this issue is a matter of balancing: balancing the principle that the legislation should be applied (hereinafter: the principle of legality) against the principles of proper administration behaviour that are involved. This approach by the Supreme Court, i.e. the approach that the administration is bound not only by legislation but also by "principles of proper administration behaviour", raises the question of how to apply this approach. In which circumstances do the principles of proper administration behaviour demand a deviation from the correct application of the legislation? If this question could indeed only be answered on a case-by-case basis without further guidelines of the Supreme Court, there would be a lot of uncertainty. However, the Supreme Court has developed a method that offers guidelines for the courts when applying the principle of legitimate expectations and the principle of equality. [28] This is the method of "priority rules". In this section, we expand on this method.

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[26] R.H. Happé, P.F.M. van Loon, J.P.F. Slijpen and M.R.T. Pauwels, *Algemeen fiscaal bestuursrecht*, Deventer: Kluwer, 2010, chapter 3.

[27] Note that the principle of legitimate expectations and the principle of equality are also principles that should be respect by the legislator. So, they are also principles of proper lawmaking. However, taking into account the subject of this contribution, we focus on these principles in their function of principles of proper administration behaviour.

[28] See, *in extenso* on the subject of weighing the principle of legality vs. the principle of legitimate expectations or the principle of equality when applying tax law, Happé 1996.

In a range of judgments, the Supreme Court has distinguished several particular types of situations ("standard situations"). These standard situations are situations with certain features that occur regularly in tax practise. For example, as concerns the principle of legitimate expectations, the Supreme Court has distinguished several standard situations in which the tax administration raises expectations to taxpayers. The distinction is based on the origin of the expectations. Standard situations are amongst others the situation in which expectations with respect to the application of the law are raised by policy rules, the situation in which such expectations are raised by an opinion of the administration and the situation in which such expectations are raised by general information provided by the administration. Also with respect to the principle of equality, the Supreme Court distinguished several standard situations.

For each type of standard situation, the Supreme Court ruled, under which circumstances, which of the competing principles (the principle of legality or the principle of proper administration behaviour involved) has more weight. In his Phd-thesis Happé introduced the concept of 'priority rule' for this method.[29] Indeed, conceptually, the Supreme Court provides a rule: if in situation P circumstances X and Y are present, then principle A supersedes principle B. In other words, the rule provides under which circumstances which principle outweighs – and therefore gets priority above – the other principle in the standard situation concerned. Happé has also noted that this approach of the Supreme Court has a sound legal theory basis, for it fits within the legal theory of Dworkin.[30]

A characteristic of a priority rule is that it has the same structure as a statutory provision. Just like a statutory provision, a priority rule sets criteria: in a specific case, it should be verified whether the criteria are all met. These criteria are particular circumstances that should be present. If the criteria of a priority rule are all met in the case at hand, the priority rule applies. In that case, the principle is applied that has priority according to the priority rule. If one of the criteria is not met in the case at hand, the

[29] Happé 1996, pp. 73-103.
[30] Happé 1996, pp. 73-103.

priority rule is not applied. In that case, the other competing principle has priority.

To illustrate this, we refer to the priority rule for opinions. This priority rule prescribes that the expectations raised by an opinion[31] are honoured where: (a) the tax inspector takes a certain position (an opinion) concerning the application of the tax law in the case at hand of a taxpayer; (b) the taxpayer has informed the tax inspector of all relevant facts and circumstances of that case; (c) the taxpayer may reasonably think that the opinion of the tax inspector is in the spirit of the law, and (d) the tax inspector is competent to deal with the taxpayer. So, in case all these requirements are met, the principle of legitimate expectations has priority above the principle of legality. Then the tax law should be applied in accordance with the expectations that have been raised, deviating insofar from the strict application of the legislation. However, if one of the criteria is not met, the principle of legality takes precedence.

As mentioned above, the Supreme Court has not only developed a system of priority rules in the field of the principle of legitimate expectations to review the behaviour of the tax administration. It has also developed a similar system (priority rules for standard situations) in the field of the principle of equality as a principle of proper administration behaviour. An example is the priority rule for the situation in which the tax administration has a certain favourable policy that has not been published.[32] If the taxpayer is able to mention 'sufficient' other cases which are comparable with his situation, the tax inspector has to declare whether such a favourable policy exists and whether the situation of the taxpayer is covered by that policy rule. If that is the case, the tax administration should in principle apply that policy rule to that taxpayer, notwithstanding that the policy rule deviates from the legislation. In other words, in that case, the principle of equality has priority over the principle of legality.

[31] As mentioned in section 2.3 this includes the so-called "promise" and the "declaration of agreement". Furthermore, the priority rule also applies to the situation in which the taxpayer has the (reasonable) *impression* of a promise by the taxpayer.

[32] As noted in section 6.2, if the policy rule is published, the Supreme Court considers this situation in the sphere of the principle of legitimate expectations and not in the sphere of the principle of equality. Theoretically, however, it would also have possible to provide legal protection via the latter principle.

5.5. Conclusion

In section 5.2 we noted that, due to the discretion of the tax administration, there is potentially the risk of an insufficient safeguard against arbitrariness of the tax administration and the risk of an infringement of the principle of legitimate expectations or the principle of equality. The reason for this is that legislative rules are inevitably not sufficient to prevent arbitrariness or such an infringement. In section 5.3 and 5.4, we have shown that the judiciary has, however, provided counterbalance and has taken care of legal protection of taxpayers. First and most importantly, the Supreme Court has acknowledged the principles of proper administration behaviour as legal norms by which the tax administration is bound. So, in fact, the Supreme Court has extended its "span of control": not only are legislative rules norms against which to review behaviour of the tax administration, but so also are principles of proper administration behaviour. In other words: the rule of law is really treated as the rule of *law*: law is not only conceived of as "a bunch of rules" but as consisting of rules and legal principles. From a more legal philosophical point of view, the concept of law is that of "law as integrity".[33] Secondly, the Supreme Court has developed a system of priority rules to deal with the weighing of the principles of proper administration behaviour and the principle of legality. This system of priority rules for standard situations ensures that the weighing of principles occurs consistently. In particular cases it should be verified whether the criteria of the priority rule concerned are met, in order to assess whether the principle of proper administration behaviour concerned has priority over the principle of legality. Interestingly, in this way, the judiciary has compensated for the shortcomings of legislative rules to prevent arbitrariness by the introduction of other rules, i.e. priority rules.

[33] See, for example, Ronald Dworkin, *Law's Empire*, Cambridge, MA.: The Belknap Press of Harvard University Press, 1986, p. 225; see also Ronald Dworkin, *Taking Rights Seriously*, London: Duckworth, 1978, p. 22.

6. Administration's binding to its own practise; some priority rules

6.1. Introduction

The above shows that, when applying the law, the Netherlands tax administration may be bound to its own practise notwithstanding the practise deviates from the strict application of the legislation concerned. The principles of proper administration behaviour are the basis for this. It should be recalled that this only applies if the administration's practise is more favourable than the legislation concerned.[34] In this section, we discuss several examples of practises to which the administration is bound when applying the law. We focus on the two most important principles in this respect, viz. the principle of legitimate expectations and the principle of equality.

6.2. Administration's practise and the principle of legitimate expectations

The analyse of case law shows that there are several types of situation ("standard situations") for which the justice considers that the administration is bound to legitimate expectations raised by its own practise. In this section, we shortly discuss the main priority rules.

First, legitimate expectations could be raised by a published policy rule (interpretative or approving). It could be that a policy rule declares an application of the law that deviates – or appears to deviate –from the correct application of the statute concerned. For this type of situation, the Supreme Court provided the priority rule that the principle of legitimate expectations outweighs the principle of legality in case the taxpayer may reasonably refer to expectations extracted from the policy rule concerned.

Secondly and thirdly, legitimate expectations could be raised by general information[35] of the tax administration or by specific information upon

[34] If the legislation concerned is more favourable than the administration's practise, the principle of legality precedes and the legislation should be applied. As this latter is less interesting, we focus on the situation in which the administration's practise is more favourable than the legislation concerned.

[35] Examples are guidelines and brochures of the tax administration and instructions that accompany the tax return forms.

request[36], concerning the meaning of a provision, without reference to the real circumstances of the taxpayer. It could be that such information raises expectation at taxpayers with respect to the application of the law which deviates from the correct application of the statute concerned. For these standard situations (expectations raised by general information or by specific information), the Supreme Court provided priority rules that are generally the same. The main rule is that, notwithstanding that the information raised expectations about an application of the law that is not correct, the principle of legality supersedes. So, based on this main rule, the expectations raised are not honoured. However, as an exception, the principle of legitimate expectation has priority if (i) the taxpayer has executed an action relying on the information, as consequence of which not only he is indebted to pay tax according to the legislation but he has also an additional loss, (ii) the information was provided by the competent authority, and (iii) the information provided was not so clear contrary to the correct application of the legislation that the taxpayer should have realized the incorrectness of the information.

Fourthly, expectations could be raised by an opinion of the tax inspector. In the situation of an opinion, the tax inspector has provided his view about the tax consequences in the concrete case at hand. By contrast, in the situation of (general) information, the tax administration only provides its general view on the interpretation or application of a statute, so apart from and without taking into consideration the concrete case at hand. Above (section 5.4), we described to priority rule for the situation of an opinion that appears not to be in line with the correct application of the statutes concerned.

Finally, it is even possible that an action of the tax inspector raises expectations by taxpayers about the application of the law, while the tax inspector was not even aware that he has raised these expectations. It concerns the situation where the taxpayer concerned gets the *impression* that the tax inspector took an opinion (so called "implicit opinion"). Note that the point of view is thus the view of the taxpayer. The general priority

[36] For example, in the Netherlands, a taxpayer cann call a special telephone number of the tax authorities (*Belastingtelefoon*) for information.

rule for this situation is that the principle of legality has priority and thus that expectations raised due to the impression by the taxpayer of an opinion of the tax inspector are not honoured. Raising the assessment in a wrongful way by the tax inspector is not sufficient for getting a justified impression. However, if there are additional particular circumstances, this might be different. For various types of situations the Supreme Court has ruled under which kind of additional circumstances the principle of legitimate expectations nevertheless outweighs the principle of legality. We discuss one type of situation for illustration purposes. This situation is that there is a tax audit, and that the tax inspector does not state anything about a certain item in the tax audit report.[37] Then, the taxpayer might get the impression that the tax administration agrees with the tax position that the taxpayer took with respect to that item in his tax return. The Supreme Court has ruled that the principle of legitimate expectations may have priority above the principle of legality where the taxpayer could have assumed that the item concerned was investigated by the tax inspector during the tax audit and that the tax inspector agreed with the tax position taken. This rule is made more concrete by the Supreme Court by considering that this will in general be the case if (i) the item concerned is relatively of such importance that it could not have escaped the tax inspector's notice and (ii) the tax consequences of the item are such that the tax inspector should have made critical remarks or should have imposed an additional assessment.

Concluding, the tax administration may be bound to its own practise, also if the practise deviates from the correct application of the statute concerned. The basis for this is the principle of legitimate expectations. Interestingly, this could not only be the case where it concerns *actual* practise of the administration, such as published policy, an opinion or (general) information. It could also be the case where the taxpayer concerned could reasonably get the *impression* of a practise, such as the impression of an opinion of the tax inspector. To be sure, the above only applies when the administration practise is more favourable than the correct application of

[37] Note that if the tax inspector states in the tax audit report that he agrees with the tax position that the taxpayer took with respect to a certain item, this would be categorized under the above-mentioned situation of an 'opinion'.

the statute. If the application of the statute is more favourable, the courts apply the statute. So, in that case, the principle of legality serves the legal protection of taxpayers.

6.3. Administration's practise and the principle of equality

6.3.1. Introduction

Besides the principle of legitimate expectations, also the principle of equality provides legal protection for taxpayers with respect to the tax administration's practise. Also here, it is a matter of balancing: balancing the principle of equality and the principle of legality. The Supreme Court has provided for priority rules with respect to this balancing for certain standard situations. In this section we shortly discuss these priority rules. First, however, it is necessary to deal with the difference between the concepts of formal equality and material equality.[38]

6.3.2. Formal equality vs. material equality

In the context at hand, formal equality refers to the fact that the tax administration should apply a tax rule consistently. A tax rule should be applied to all cases that fall within the scope of that tax rule. Likewise, if the tax administration has a certain administrative practise, e.g. a policy rule, the practise should be applied to all taxpayers whose cases fall within the scope of that practise. The principle of formal equality is therefore at stake if an advantageous practise of the tax administration is not equally applied to all taxpayers. Concluding, formal equality relates to the consistent application of rules or a practise.

Material equality on the other hand relates to the contents of a rule (or practise). Rules inherently make distinctions between groups. A tax rule for entrepreneurs makes a distinction between taxpayers that are entrepreneurs and taxpayers that are not entrepreneurs. Material equality concerns the question whether the distinction made by a rule does not violate the principle of equality. Indeed, the principle of equality requires that equal cases should be treated equally, or in other words equal cases should not be treated unequal without a reasonable justification. For the

[38] Happé 1996, pp. 289-291.

question whether or not cases are equal, the purpose of the rule concerned is relevant. It should be established whether the case that does not fall under the scope of a rule is equal – from the view of the purpose of the rule – to cases that do fall under that scope. If the answer is affirmative *and* there is no justification for the resulting unequal treatment, the principle of (material) equality demands that the rule should also be applied to the case that does not fall under the scope of the rule according to its wording. The same applies, mutatis mutandis, to an administration's practise that results in an (unjustified) unequal treatment of equal cases. Concluding, material equality may demand that the scope of a rule (or practise) is widened. So, material equality relates to the contents of a rule (or practise): the question is whether the scope of a rule is not too narrow in the sense that a rule does not include certain cases that are equal to cases that do fall within the scope of the rule.

6.3.3. Priority rules for formal equality

With respect to the principle of equality in the sense of formal equality the Supreme Court has provided three priority rules.

The first priority rule concerns the situation of approving, non-published, policy. If the competent tax inspector has a certain approving, non-published, policy, he should apply this policy to all taxpayers that fall within the scope of the policy. If the tax inspector however deviates from this policy at a disadvantage of a taxpayer, the priority rule is that the court should set the correct application of the statute aside and apply this policy also to this taxpayer. Note that from a theoretical point of view it would be expected that a comparable priority rule for an approving policy rule that is published. Indeed, the Supreme Court provides for legal protection for taxpayers in that situation. However, the Supreme Court does so not via the principle of equality, but via the principle of legitimate expectations. We refer to the appropriate priority rule that is mentioned in section 6.2.

The second priority rule concerns the situation in which the competent tax inspector treats one or more persons of a group of persons in a comparable situation favourable (compared to the correct application of the law) with

the objective of favouritism. For this situation the priority rule[39] holds that the correct application of the statute should also be set aside with respect to the other persons of the group and that these other persons should also get the favourable treatment. We remark that the requirement of an 'objective of favouritism' is a high barrier in practise. This rule has seldom been applied.

The third priority rule concerns the situation in which the competent tax inspector has not applied the statute concerned correctly – but more favourable – with respect to the majority of a group of persons in a comparable situation.[40] For this situation the so-called "majority rule" holds that the correct application of the statute should also be set aside with respect to the other taxpayers of the group. It should be noted that a characteristic of this situation is that there is no (approving) policy of the inspector. The situation has a pure quantitative nature: the key issue is whether the tax inspector has not applied correctly the statute concerned to the majority of the group.[41]

6.3.4. Priority rules for material equality

The Supreme Court has also provided for priority rules with respect to the principle of equality in the sense of material equality. These priority rules concern especially policy rules or policy practises of the tax administration. In that respect, the distinction between published and non-published policy rules appears not to be relevant. The same rules apply to them. Instead, case law shows that a distinction should be made between approving policy rules on the one hand and interpretative policy rules and practises on the other hand.

As shown above (section 2.2), in case of an approving policy rule the tax administration approves – in favour of taxpayers – a certain application of the tax legislation in a specific situation even though this application

[39] This rule is called the rule of the objective of favouritism.

[40] We focus on the main line of the rule. The rule itself is far more complex as the Supreme Court has developed a lot more additional rules to fill in the main rule, e.g. with respect to the issue which cases qualify and count as cases in which the statute is not correctly applied.

[41] As mentioned in the previous footnote the Supreme Court elaborated the majority rule in a very detailed way. As a consequence, it is factually very difficult for a taxpayer to meet all the subcriteria.

deviates from the strict wording of the statute concerned. In case of an approving policy rule – either published or non-published – the priority rule for material equality holds, with respect to a case that does not fall under the scope of the approving policy rule concerned, that the correct application of the statute should also be set aside if (i) the approving policy rule involves an unequal treatment of equal cases and (ii) there is no justification for this unequal treatment. It these two criteria are met, the approving policy rules should also be applied to the case at hand. So, the scope of the approving policy rule is extended via the principle of equality.

In case of an interpretative policy rule or practise, the tax administration has a policy with respect to the way a particular statute should be applied to a certain type of situation based on a certain interpretation of that statute, of which the administration believes it is the correct interpretation of that statute. It might appear however that this interpretation is not correct and that the interpretation was more favourable for the taxpayers concerned than the correct interpretation of the statute. Often, this implies that these taxpayers were treated more favourable than other taxpayers whose cases did not fall within the scope of that policy but which are – from the viewpoint of the correct interpretation – equal to the cases to which the policy is applicable. The question arises whether these latter taxpayers may successfully invoke the principle of equality (material equality) to also obtain the favourable treatment of the policy.[42]

The Supreme Court has answered this question negatively in a landmark case in 1997.[43] Its considerations are interesting from a methodological perspective. The Supreme Court first states that these taxpayers have in principle the right to the same favourable treatment based on the principle of equality. Subsequently, however, the Supreme Court balances the principle of equality against the principle of legality, and rules that the latter principle gets priority under certain conditions. The resulting main priority rule holds that if there is policy that only applies – based on its objective –

[42] Note that the taxpayers that fall within the scope of that policy still have the legal protection that the (favourable) policy is applied to them, notwithstanding that the policy is based on an incorrect legal view. This is based either on the principle of legitimate expectations in case the policy is published (see section 6.2) or on the principle of equality in the sense of formal equality (see section 6.3.2).

[43] Supreme Court 5 February 1997, no. 31312, BNB 1997/160.

to a certain group of cases with a special feature, and that is based on an incorrect legal view that relates to that feature, there is no legal obligation for the tax administration to apply this policy also to the cases that do not belong to that group but that are for the rest equal from the view of the application of the statute concerned. [44] The ratio of this priority rule is that the tax authorities are "allowed" to make a mistake as regards the interpretation of a statute, without being "punished" by a proliferation of the mistake via the principle of equality.

However, there is also an accompanying priority rule: if the tax administration however continues the policy after it woke up – for example due to a judicial decision or own insight – that the policy is based on an incorrect legal view, then the policy should be also applied to these latter cases.[45] In our view, this accompanying priority rule is logical. Indeed, if the tax administration continues policy that is originally interpretative, although it knows that the policy is not in line with the correct interpretation of the statute concerned, the policy gets a different character as from that moment. The policy is not 'interpretative policy' anymore but becomes 'approving policy'.

A very special situation concerns the *Vinkenslag*-case. The tax administration has concluded certain agreements with people that lived on the caravan camp 'Vinkenslag' with respect to their taxation. Reasons for these agreements were that it appeared to be difficult for the tax administration to obtain information from these people that is relevant for the taxation as well as to collect taxes from these people. The exact contents of these agreements are not very clear, but there are indications that the tax treatment based on these agreements was very favourable for the people of the caravan camp. This became known in public, and some other taxpayers took the position – based on the principle of equality – that they should be treated in a similar (favourable) way. However, the Supreme Court dismissed this appeal. Interestingly, in its considerations, the

[44] Supreme Court 5 February 1997, no. 31312, BNB 1997/160 and Supreme Court 22 January 2010, no. 09/01038, BNB 2010/146.

[45] Supreme Court 22 January 2010, no. 09/01038, BNB 2010/146.. It should be noted that the Supreme Court noted that a certain transition period might be applied before the policy is terminated. Within this transition period (that should not be unreasonable long) this accompanying priority rule does not apply but the main priority rule applies.

Supreme Court showed first its disapproval with respect to the agreements concluded by the tax administration with the taxpayers of the caravan camp 'Vinkenslag'. The Supreme Court has considered:

"these (…) agreements are connected with the fact that the these taxpayers [of the caravan camp; RH/MP] put obstacles for enforcement of the law; *this fact should not have been considered relevant for the levying of taxes*." (*italics* added)

Subsequently, the Supreme Court has ruled that the appeal on the principle of equality is not successful. The Court considered:

"The principle of equality, as a principle of proper administration behaviour, goes not that far that when the administration realizes that it has pursued a policy with respect to a certain group of taxpayers that implies a preferential treatment of these taxpayers which is unjustifiable, it should also provide to others an equal, even unjustifiable, advantage. The legal obligation to comply with the principles of proper administration behaviour requires in such a case that the unjustifiable favourable treatment should be terminated instead of extended. If it is decided to such termination, others cannot successfully invoke the principle of equality."

Note that the Supreme Court again shows its disapproval with respect to the 'Vinkenslag'-agreements by remarking – in the second sentence – that there is a legal obligation to end the unjustifiable favourable treatment.

7. Final observations

7.1. Concept of administration practise

With reference to case law of the CJ, the editors of this journal raised the question what is the definition of the concept of tax administration practise in the Netherlands. However, there is no well-delineated comprehensive definition of tax administration practise in the Netherlands tax case law. Unlike perhaps in the sphere the CJ has to rule, there is no real need in the Netherlands case law to have such a comprehensive definition.

Instead, in the Netherlands situation it is more important to establish *which kind* of tax administration practise is at hand, where there is some kind of tax administration practise. The kind of the tax administration practise is important because the legal consequences differ depending of the kind of

tax administration practise. For example, if a taxpayer appeal to the principle of equality in the sense of material equality with respect to a policy of the tax administration, it is relevant whether the policy concerned is 'approving policy' or 'interpretative policy' (see section 6.3.3).

The above analysis shows that there are *various kinds* of tax administration practises, such as approving and interpretative policy – which could be published or non-published –, 'opinions' delivered by the tax inspector, the possibility to conclude settlement agreements as well as the method of concluding 'enforcement agreements' by the tax authorities with taxpayers to promote compliance (see section 2).

Further, it appears that there are *different levels* at which the practises are pursued. For example, practises may be established at a general level, namely the level of the State Secretary of Finance, e.g. approving policy rules that are published. Practises may however also be established at a very concrete and individual level, for example where, upon request of a taxpayer, the tax inspector provides his opinion on the tax consequences of a certain transaction.

Moreover, it might also be that there is a *deemed* tax administration practise. We discussed two situations of such deemed tax administration practise to which legal consequences are attached. The first is the situation to which the so-called "majority rule" applies, which priority rule is provided in the sphere of the principle of equality in the sense of formal equality (see section 6.3.2). The second situation concerns the situation where the taxpayer gets the *impression* that the administration took an opinion. Under circumstances, the administration should honour the legitimate expectations raised by such an "implicit opinion", based on the principle of legitimate expectations (see section 6.2).

7.2. Boundaries to the tax administration's contra legem application of the law

In strictly formal terms, the Netherlands tax administration has no discretionary power when applying the tax legislation (besides some minor exceptions). Tax statutes usually do not grant discretion to the

administration. However, in section 2 we showed that the tax administration factually has discretion.

Further, as discussed in section 3.2, the Supreme Court confirmed that the Netherlands tax administration indeed could have competence to provide additional (policy) rules and thus has insofar some formal discretionary power. In section 3.3, we argued that if a tax administration practise deviates (in favour of taxpayers) from the strict wording of the statute concerned, this not always implies that this practise should be qualified as genuinely *contra legem*. The deviation of the strict wording of the statute could happen with the purpose to do justice to the peculiarities of the cases concerned. If this is the case and this purpose to do justice is in line with the goal and the underlying principles of the statute concerned, the administration practise is *intra jus* and should not be qualified as genuinely *contra legem* but as *praeter legem*. As discussed in section 3.3, the same applies, *mutatis mutandis*, to other ways the tax administration uses its factual discretion when applying the law, e.g. in case of an "opinion".

Concluding, with respect to the question whether or not the tax administration stays within the limits of the law when exercising its discretion (deviating from the strict wording of the statute concerned in favour of taxpayers), it is decisive whether the application concerned is in line with the underlying goal and principles of the statute concerned. If this is not the case, the tax administration has exceeded its competence in this respect. Then, the line between intra jus and extra jus has been crossed. In section 6.3.3, we have discussed a very clear example of a situation in which the tax administration did exceed its competence and entered into the *extra jus* and *contra legem* zone. This is the situation to which the *Vinkenslag* case relates. In a case in which another taxpayer claimed – referring to the principle of equality – the same treatment as the people of the Vinkenslag caravan camp, the Supreme Court showed his disapproval of the conduct of the tax administration. Furthermore, it should be emphasised that the question whether or not the tax administration has exceeded its competence should not be mixed up with the question whether the taxpayers have legal protection. An example is the situation in which the competent tax inspector treats one or more persons of a group of persons

in a comparable situation favourable with the objective of favouritism. As discussed in section 6.3.3 the applicable priority rule – based on the principle of equality in the sense of formal equality – holds that also the other persons of the group should also get the favourable treatment. Nonetheless, this does not imply that the favourable treatment is intra jus and praeter legem. The treatment *itself* is contra legem, but the other persons should nevertheless get an equal treatment because of the principle of equality.

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