



# JUDGE OF THE CONSTITUTIONAL COURT

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## SEPARATE OPINION

of the Justice of the Constitutional Court

Aldis Laviņš

in Riga, 2 November 2017

in Case No. 2016-14-01

**“On Compliance of Section 3, 5, 6, 7 and 9 of the law “On Solidarity Tax” with the First Sentence of Article 91 and Article 109 of the *Satversme* of the Republic of Latvia”**

1. On 19 October 2017, the Constitutional Court passed the judgement in Case No.2016-14-01 “On Compliance of Section 3, 5, 6, 7 and 9 of the law “On Solidarity Tax” with the First Sentence of Article 91 and Article 109 of the *Satversme* of the Republic of Latvia” (hereinafter – the Judgement).

**I cannot uphold the arguments included in the Judgement that were the basis for the finding that the differential treatment, which was established by Section 6 of the law “On Solidarity Tax”, lacked a legitimate aim.**

In providing reasoning for my opinion, I shall use the abbreviations used in the Judgement.

2. It is validly found in the Judgement that:

1) differential treatment of the payers of solidarity tax has been established, i.e., different tax rates have been established for them (*see Para 24 of the Judgement*)

2) differential treatment has been established by law (*see Para 25 of the Judgement*).

Upon identifying differential treatment, the Constitutional Court must examine, whether such treatment has a legitimate aim. In the legal proceedings before the Constitutional Court, if restrictions on fundamental rights have been imposed, the institution, which has issued the contested acts, has the obligation to present and substantiate the legitimate aim of the restrictions that have been established. (*see, for example, Judgement of 13 June 2014 by the Constitutional Court in Case No. 2014-02-01, Para 13*).

In the case under review, the *Saeima* stated in its written reply that the contested norms were aimed at decreasing the regressivity of tax burden, ensuring that the payers of the solidarity tax participate, in a fair amount, in covering the costs of measures for decreasing social inequality. Whereas the procedure for administrating the solidarity tax that is linked to the state social insurance system had been chosen because it was simple and major state budget resources had not been required to introduce it. Moreover, allegedly, it does not create an additional administrative burden for the taxpayer (*see Written Reply by the Saeima, Case Materials, Vol. 4, p.22*).

At the court hearing, in which the participants of the case participated, the representatives of the *Saeima* drew attention to the fact that the procedure of administering the solidarity tax was oriented towards effectiveness since the revenue into the state budget was ensured each month and could be forecasted without separate administrative costs. The representatives of the *Saeima* mentioned the ensuring of public welfare in an effective way without spending disproportionate resources for a new model of tax administration as the legitimate aim, envisaged in Article 116 of the *Satversme*, which was said to justify the differential treatment caused by the tax rates set in Section 6 of the law

“On Solidarity Tax” (see *Transcript of the Court Hearing of the Constitutional Court on 5 September 2017, p. 61*).

3. In the Judgement, the Court has noted that in exercising its discretion in the field of taxation policy, the legislator must comply with the principles of effectiveness, justice, solidarity, and timeliness. (see *Para 26 and Para 27.3. of the Judgement*). I am of the opinion that in the Judgement, in assessing whether the differential treatment has a legitimate aim, the issues linked to complying with the principles of effectiveness and solidarity were not duly examined. It was important to consider these issues in the case under review, in analysing the course of introducing the system for administering the solidarity tax that comprised the different tax rates and in taking into account the legitimate aim defined in Article 116 of the *Satversme* – protection of public welfare.

3.1. The conclusion made in Para 27.3. of the Judgement that the differential treatment of the groups of payers of solidarity tax, established in Section 6 of the law “On Solidarity Tax”, lacked a legitimate aim, essentially, is based only upon the conclusion that the simplicity of administering a tax could not be the only objective grounds for establishing differential treatment.

One of the legitimate aims indicated in Article 116 of the *Satversme* – protection of public welfare – is a complex concept, in the context of which the effectiveness of a tax cannot be viewed only from the vantage point of the simplicity of its administration. I.e., effectiveness and simplicity are not identical terms.

The differential treatment caused by the different tax rates envisaged in the law “On Solidarity Tax” has been established with the aim of decreasing in a solidary way the regressivity of tax burden (persons with higher income have lower taxes) in a way by which tax payments would effectively, regularly and clearly ensure the necessary revenue into the state basic budget. The linking of the respective procedure for administering the tax to the system for administering the mandatory social insurance contributions is aimed at predictable collection of

the tax every month, and these tax payments can be used for decreasing inequality or the differences between the welfare levels among inhabitants.

It is obviously clear that if the legislator were to establish other rates of solidarity tax and would not link the procedure for administering this tax to the system of the state social insurance sizeable state budget resources would be needed to establish a new mechanism for administering this tax. Secondly, the administrative burden would increase for both employers and employees, since the solidarity tax would have to be calculated separately and, submitting tax returns in set terms, the transfer of the tax into the state basic budget would have to be ensured. Moreover, many payers of the solidarity tax work with two or even several employers. This means that without ensuring a complex system for sharing information for a large part of the payers of this tax it would be impossible to determine, whether and when the obligation to pay the solidarity tax has set it, and, in certain cases, it would be necessary to reimburse the overpaid amounts.

The Constitutional Court has found that the State has the obligation to establish an effective system for collecting taxes in the interests of public welfare (*see Judgement of 15 April 2015 by the Constitutional Court in Case No. 2012-18-01, Para 17*). The chosen solution for administering the solidarity tax complies with the aforementioned finding by the Constitutional Court; i.e., it is effective and rational since it imposes the obligation upon the Agency to keep the records of the tax and to determine the part of payment, which is the solidarity tax and, thus, is to be transferred into the state basic budget. Moreover, this solution does not envisage any additional administrative burden either for the employer or the employee.

Thus, a different procedure for administering the solidarity tax would not foster its effectiveness, regularity and predictability and would not be aimed at the protection of public welfare to the same extent as the solution that is in force.

**3.2.** The legislator may protect public welfare by exercising its discretion in the field of taxation policy and abiding not only by the principle of effectiveness but also by the principle of solidarity.

Before the solidarity tax was introduced, when an employee's remuneration reached the maximum amount of the object of social insurance contributions the burden of labour tax decreased both for the employer and the employee. The annotation to the draft law "On Solidarity Tax" indicates that the burden of labour tax for the persons, who received the minimum monthly salary defined by the Cabinet, and the persons, whose monthly salary was 10 000 *euro*, differed by almost 8 per cent. This means that for persons who received the minimum monthly salary the burden of labour tax was almost by one fifth higher than for persons with much higher monthly salary.

The introduction of the solidarity tax ensured that the burden of taxes to be paid from all income gained in salaried work and from income of a self-employed person, which exceeded the maximum amount of the object of social insurance contributions, did not decrease but remained the same as for the persons, who had not reached this maximum amount. The tax rates, which are introduced by Section 6 of the law "On Solidarity Tax", are different for different persons; however, they are aimed at decreasing the regressivity of the labour taxes, i.e., retaining a similar burden of labour taxes for all groups of taxpayers. For example, upon reaching the maximum amount of the object of social insurance contributions, the burden of labour taxes does not decrease also for such an employee, who has already reached the age, when he is entitled to the state old-age pension. Thus, the social inequality is reduced and the principle of socially responsible, reciprocally solidary society is embodied.

In view of the above, it must be concluded that the linking of the procedure for administering the solidarity tax to the system for administering the mandatory social insurance contribution, in addition to effective and predictable collection of the tax into the state basic budget, allows decreasing the regressivity of the tax burden, ensuring that equal tax burden is maintained in all social groups. By this, the principles of effectiveness and solidarity are abided by in the national taxation policy. The choice of other solidarity tax rates or other procedure for calculating or administering it would be less compatible with these principles.

**3.3.** At least four conditions that are linked to the protection of public welfare are indicated in Para 27 of the Judgement:

- 1) simplicity of administering the tax;
- 2) significant amount of budget revenue (the fiscal effect of the tax);
- 3) low administration costs;
- 4) small number of payers of the administrative tax.

In the Judgement, with respect to each of these conditions separately it has been, essentially, found that these *per se* cannot be used to substantiate the restriction on fundamental rights in the meaning of the first sentence of Article 91 of the *Satversme*. However, as the Judgement reveals, several of these conditions were present rather than just a sole one.

**In view of the above, there were grounds to find in the case under review that the differential treatment of the groups of payers of solidarity tax, established by Section 6 of the law “On Solidarity Tax”, had a legitimate aim – protection of public welfare.**

**4.** The specificity of tax law influences the scope of constitutional review and the methodology for examining the constitutionality of the contested norm of the tax law. To establish, whether the restriction on fundamental rights caused by the obligation to pay a tax complies with Article 91 of the *Satversme*, it must be verified, whether the different solidarity tax rates have a reasonable explanation, based on objective and rational considerations; i.e., whether the principle for calculating the tax has not been set arbitrarily (*compare to Judgement of 25 March 2015 by the Constitutional Court in Case No. 2014-11-0103, and Judgement of 3 July 2015 in Case No. 2014-12-01*).

Although the linking of the different tax rates to the system for administering the mandatory social insurance contributions is aimed at complying with the principles of effectiveness and solidarity, the legislator, nevertheless, has to provide objective and reasonable arguments regarding the tax rates *per se*. Different tax rates have been set for payers of the solidarity tax –

employees, depending upon the types of social insurance that the particular person is insured for; however, the amount of solidarity tax rates cannot be substantiated by social insurance risks since the solidarity tax has other aims. Moreover, from the perspective, of whether the different tax rates can be reasonable explained, the fact that these rates have been defined precisely, up to the hundredth part of a per cent, is not insignificant. Likewise, the amount of these rates was different in 2016 and 2017.

I am of the opinion that in the course of hearing the case the legislator has not provided an explanation, based on objective and reasonable considerations, regarding the particular rates of the solidarity tax applied to various groups of persons and the differences between them. The arguments included in Para 26 and Para 27 of the Judgement could have been used to arrive at the aforementioned conclusion.

**Hence, the differential treatment caused by Section 6 of the law “On Solidarity Tax” is incompatible with Article 91 of the *Satversme*.**

5. In addition, I draw attention to the fact that the Applicants have singled out three independent aspects, in which, in their opinion, the contested norms are incompatible with the principle of legal equality included in the second sentence of Article 91 of the *Satversme* (a precise account of these aspects is provided in Para 2 of the Judgement). One of these aspects is linked to the consideration that a self-employed person may choose the income, from which to make social insurance contributions, as well as change the object of contributions once per quarter, whereas an employee has no opportunity of choosing the object of insurance contributions. Such procedure of paying the solidarity tax is said to cause a violation of the equality principle.

The Constitutional Court has analysed the procedure for keeping record of a person’s income both for an employee and a self-employed person, as well as the procedure for paying the social insurance contributions and the solidarity tax and has found that with regard to the obligation of paying the solidarity tax both

employees and self-employed persons, who have the obligation to pay this tax, are in comparable circumstances.

However, in the following text of the Judgement, it is not examined, whether such procedure for paying the solidarity tax, in compliance with which, as noted in the applications, one group of persons – employees with income that exceeds the maximum amount of mandatory insurance contributions – has no right to choose the object of the social insurance contributions and, thus, the obligation to pay the solidarity tax sets in, whereas another group of persons – self-employed persons with income that exceeds the maximum amount of mandatory insurance contributions – has the right to define the object of social insurance contributions, even such that does not cause the obligation to pay the solidarity tax, is compatible with the principle of legal equality included in Article 91 of the *Satversme*. In the absence of such examination, the conclusions made in Para 22.2. are not of essential significance.

Justice of the Constitutional Court

A. Laviņš