THE CONSTITUTIONAL COURT
OF THE REPUBLIC OF LATVIA

JUDGMENT

ON BEHALF OF THE REPUBLIC OF LATVIA

Riga, April 3, 2008

in case No. 2007-23-01

The Constitutional Court of the Republic of Latvia, composed of the Chairman of the Court session Gunārs Kūtris, Justices Kaspars Balodis, Juris Jelāgins, Kristīne Krūma and Viktors Skudra,

having regard to the application of the Department of Administrative Cases of the Supreme Court Senate of the Republic of Latvia (hereinafter – the Applicant),

based on Article 85 of the Satversme (Constitution) of the Republic of Latvia and Item 1 of Article 16, Item 9 of the first part of Article 17 and Articles 19.[1] un 28.[1] of the Constitutional Court Law,

on March 4, 2008, in the Court Session examined the case in written proceedings

"On Compliance of the Words "not More Often than Once per Three Years" of the First Part of Section 33.1 of the Law "On Taxes and Fees" (Wording of the Law of April 13, 2000) with Article 1 of the Satversme (Constitution) of the Republic of Latvia".

The Constitutional Court has established:

1. The Saeima of the Republic of Latvia (hereinafter – the Saeima), on February 2, 1995, passed the Law "On Taxes and Fees" (hereinafter – the Tax Law), and it came into

force on April 1, 1995. This Law provides for general principles of application of taxes in the State, as well as it provides for liability for violation of tax laws. One of the kinds of the liability, that has been included in the law already since its coming into force is imposition of fines.

Section 33.1 was included in the Tax Law on April 13, 2000 when the Saeima adopted the Law "Amendments to the Law "On Taxes and Fees"". The first part of the abovementioned Section provided:

"The tax administration in evaluating the essence and nature of the violation of the taxpayer, the fact of how many times the violation has been committed, the harm caused and the integrity of the taxpayer in cases where the taxpayer has disputed the decision of the tax administration, has the right to reduce the fine imposed as a result of controls (tax verifications (audits) and examinations), but not more than 70 percent of the amount and not more often than once per three years."

This provision came into force on May 17, 2000.

On March 31, 2004, the Saeima adopted the Law "Amendments to the Law "On Taxes and Fees"" with the following wording of Section 33.1:

"The tax administration in evaluating the essence and nature of the violation of the taxpayer, the fact of how many times the violation has been committed, the harm caused and the integrity of the taxpayer in cases where the taxpayer has disputed the decision of the tax administration, has the right to reduce the fine imposed as a result of controls (tax verifications (audits) and examinations) up to 70 per cent of the amount, but not more often than once a year."

This provision was effective from May 1, 2004 up to January 1, 2007, when Section 33.1 was excluded form the Tax Law by the Law "Amendments to the Law "On Taxes and Fees" of October 26, 2006.

2. The Applicant indicates that application of the words "but not more often than once per three years" (hereinafter – the Contested Provision) causes violation of the principle of proportionality, and consequently – that of the principle of justice in the cases when the imposed fine is non-commensurate with the violation committed. In the practice, there often occur cases when a taxpayer may not be considered as an ill-intentioned nonpayer of taxes, since he or she has acted inattentively by, for instance, including pre-tax

into the declaration two days earlier, which according to the Law shall be included in the declaration only the following month. The objective of the legislator has not been to place in an equal situation and to equally punish such taxpayer who evades taxation and such taxpayer who has indicated the entire taxable value in the declaration.

According to the viewpoint of the Applicant, the legislator has adopted an imperative provision of law by also including therein a typical case. Consequently, it is impossible for the authority, nor for the Court to decide on the most appropriate legal consequences but it is necessary to follow the provision of the law that does not allow reducing the fine if it has been done once in the respective period. This objective of the norm does not per se comply with the principle of proportionality and justice and hence it automatically means violation of Article 1 of the Satversme of the Republic of Latvia (hereinafter – the Satversme).

In the Application there is information provided that Section 33.1 of the Tax Law shall be applied in the administrative courts during several more years taking into account the fact that the administrative acts issued in 2003 and 2004 are still being examined. Therefore assessment of compliance of this norm in the Constitutional Court would be necessary, and in the case of establishing non-compliance it would be necessary to cancel the norm from the moment of adoption thereof. This would allow the administrative courts to apply the principle of proportionality and justice also in the cases when the fine has already been imposed once in the respective period.

When objecting to what has been indicated in the reply of the Saeima, The Applicant emphasizes that reducing of a fine must not depend only on the fact whether the violation has been done for the first time or repeatedly. Recommitment of tax violations may cause doubts regarding honesty of taxpayers; however this must be assessed individually in each case. Also, according to the viewpoint of the Applicant, in the case of repealing of the provision, a positive regulation would be necessary.

When assessing the possibility to apply the latest regulation of the Tax Law in the particular administrative case regarding reducing of a fine, the Applicant holds that Section 33.3 of the Law is not favourable for taxpayers. Namely, the latest regulation, unlike Section 33.1 of the Tax Law, provides for additional requirements regarding reducing of a fine, including the main – a taxpayer agrees to the additionally calculated amount of tax.

Moreover, when referring to the legal doctrine of Germany, it is indicated that in the field of tax rights it is also possible to apply such legal norm that is effective during the period when the respective decision has been adopted in the authority.

3. The institution that has passed the contested act – the Saeima – holds that the application is ungrounded and the Contested Provision complies with the Satversme.

Before coming into force of the Contested Provision – May 17, 2000 – the responsibility for reducing of the tax base was provided by Section 32 of the Tax Law. It provided that in the case if a taxpayer in violating the requirements of tax laws, in declarations submitted to the tax administration or in assessment of taxes reduces the tax base (the taxable item) and the tax amount assessed from such, the tax administration shall assess and recover for the benefit of the budget from the taxpayer the reduced tax amount and a fine to the amount of such if another amount for the fine is not provided in specific tax laws. Consequently, this legal provision imperatively provided that reducing of the tax base is finable at the same amount or at the amount of 100 percent from the unpaid (missing) tax amount.

Both, the competent authorities and the legislator have established that this inflexible approach is not correct. In such cases a person could be severely fined without reason even for making a mistake. Therefore, on April 13, 2000, the Saeima adopted the Law "On Amendments to the Law "On Taxes and Fees", according to which the Tax Law was supplemented by Section 33.1 that provided for the rights of the tax administration to reduce the fine imposed. Simultaneously the legal norm also provided for restricting provisions to reduce the fine – not more than at the amount of 70 percent and not more often than once per three years.

The Saeima informs that the Contested Provision was introduced taking into consideration the provision of the first part of Section 23 of the Tax Law, namely, that the tax administration has the right, after a tax review (audit), to adjust the amount of taxes and to impose fines within a period of three years after the payment time period specified by law if the tax regulations regarding State fees have been violated. It has also been taken into consideration that the audits for taxpayers have initially been planned and carried out once per three years. Therefore it has not been necessary to

systematically provide for a possibility to reduce the fine imposed more often than once per three years.

It is also necessary to be taken into consideration that the Contested Provision can be substantiated by those interconnections that follow from other norms of the Tax Law. Namely, before May 17, 2000, Section 33 of the Tax Law provided that in the case if a taxpayer within a three year period has repeatedly violated tax laws (reducing the tax base, not declaring income or declaring less income, or has substantiated non-justifiable expenses with documents), the tax administration shall recover from the tax payer the unpaid (missing) tax amount and fine to double the extent of this amount. It is possible to conclude form this provision that violation of tax laws within the period of three years shall be qualified as a graver crime – the one that has a systematic or repetitive nature, and the fine for it shall be determined at the double amount of the unpaid (missing) tax amount. Therefore the Saeima emphasizes that according to the legal norms effective at that time reducing of the fine imposed more often than three times per three years would come into a systematic conflict with other legal norms, which would qualify such violations as a repetitive action that shall be additionally finable.

The Saeima holds that during the validity of the Contested Provision the restrictions (conditions) included therein where proportionate if the controls (audits) or inspection of a particular person has not been carried out more often than one per three years. The Saeima indicates: if the abovementioned controls have not been carried out, it was impossible to impose a fine. However, if the Contested Provision is analysed from the modern viewpoint by taking into consideration the latest amendments to the Tax Law, as well as the present administrative practice and positions of implementation of human rights, the Contested Provision may seem non-compliant to the principle of proportionality and the principle of justice. Still, first of all, the requirements of the principles of proportionality and justice in each branch or sub-branch (field) of law may differ. Second, the Contested Provision is closely related to the legal norms effective at that time and the viewpoints regarding application of legal principles dominating at that period. The Contested Provision has been regarded as progressive because it was for the first time when a norm provided for a possibility to decide on reducing a fine by assessing the nature of the violation made by a person.

It is also necessary to take into consideration that, when recognizing the Contested Provision as invalid antedate as it is asked by the Applicant, it might allow certain persons to reduce the fine for an indefinite number of times by thus disrupting the mutually coordinated system of legal norms previously effective and by placing certain persons in a more favourable situation if compared to others, for whom reducing of a fine is regulated by other legal norms adopted at a later period.

The Saeima also indicates that "recognition of the Contested Provision as invalid would not solve all necessary problems, because a judgment of the Constitutional Court would, in fact, require a positive regulation from the legislator and probably revision of other legal norms effective at that time".

Therefore the Saeima asks to recognize the Contested Provision as compliant with Article 1 of the Satversme.

4. The State Revenue Service (hereinafter – the SRS) indicates that up to May 17, 2000, the tax administration was not entitled to reduce the fine imposed in the result of controls. Hence, the fine at the equal amount of unjustly reduced tax amount was applied to taxpayers unless the certain tax laws do not provide for another fine amount. Taxpayers are basically fined at the amount of 100 percent even if the violation has been caused due to a mistake or failure of understanding the law.

Section 33.1 of the Tax Law has allowed the tax administration to assess whether the calculated fine is proportionate with the gravity of the violation, as well as it was entitled to reduce the fine up to 70 percent. Such reducing of the fine shall be qualified as application of relief if the nature and the essence of a particular violation testifies about unconscious action of a taxpayer.

The relief included in the abovementioned section has been related with the first part of Section 23 of the Law. Namely, the tax administration has the right, after a tax review (audit), to adjust the amount of taxes and to impose fines within a period of three years after the payment time period. Moreover, audits for taxpayers are planned and carried out once per three years.

This relief was considerably broadened by amendments to Section 33.1 of the Tax Law that came into force on May 1, 2004, namely, it could be applied not more often than once per year. Such changes are related with the fact that the SRS has adopted risk

management in tax administration by selecting taxpayers for carrying out tax audits. Consequently, the number of those taxpayers, for who tax assessment controls are carried out more often than once per three years, has increased.

The first part of Section 33.1 of the Tax Law has restricted the rights of the tax administration to reduce the fine imposed more often than once per three years (then – once a year). However, the tax administration has revised the issue of reducing of a fine based on the request of the taxpayer in order not to exclude the possibility to reduce a fine imposed on taxpayers during the controls for violations established in further controls.

The SRS additionally informs that during the time period from 2002 to 2006 the general manager of the SRS has reviewed 1100 applications by taxpayers regarding reducing of fines imposed in the result of the controls. The abovementioned fine was reduced for 647 taxpayers, mainly at the amount of 70 percent.

5. The Ombudsman of the Republic of Latvia (hereinafter – the Ombudsman), when referring to the jurisprudence of the European Court of Human Rights (hereinafter – ECHR), indicates that the Contested Provision restrict the rights of persons to a just court because it does not provide for a possibility to review the fine imposed on the person and to reduce the sanction imposed relative to the nature and essence of the violation. Such restriction of rights is less favourable for a person if compared to the area of regulation of the criminal procedure. Namely, the criminal procedure does not provide for any restrictions of this kind when reviewing applications regarding reducing of a fine. No such restrictions have been established even in relation to revision of the decisions lately adopted regarding reassessment of fines, for instance, in the case of new-found circumstances. The fact that a person has once taken advantage of his or her rights to refer to the nature and essence of the violation in a certain period of time in order to reduce the fine imposed without excluding existence of such rights in relation to other similar circumstances. For instance, when a person finds out new objective considerations regarding the violation (fast reassessment of taxes etc.) or a certain person has testified by means of his or her action that the fine has not been adequate or it has already reached its objective (a person, by observing the legal regulation of the field of taxes, has proved that the violation was not ill-intentioned).

The Ombudsman holds that the objectives of the Contested Provision can be reached by means of other, less restrictive measures. It has been confirmed by the legislator by

offering new wording of the Contested Provision on March 31, 2004, wherewith the time period, during which the times of reducing a fine are restricted, has been shortened. There are no data at the disposition of the Ombudsman that would make it consider that such legal regulation would threaten the possibility to ensure tax collection and prevent tax evasion. Moreover, the Ombudsman does not seed any obstacles for the fact that the objectives of the Contested Provision might be reached not only by means of shortening of the formal timeframe restriction, but also by simply carrying out the activities that fall within the scope of the competent authority, for instance, by establishing whether there exist an objective grounds for reducing a fine that has not bees assessed during the previous reassessment, if it has been carried out.

It has also been indicated that it would be useful to take into consideration also the requirements of efficiency and control of the administrative procedure that follows form the principle of good administration, when assessing the Contested Provision. This control should be ensured in the authority and the Court, and the authority may not restrict its participation in implementation of the principles of administrative procedure by formally referring to the fact that the case would be assessed by a court. It would not comply with the requirement of ensuring State administration efficiency, according to which it is possible to achieve, by letting a person to efficiently exercise his or her rights in the field of State administration at full extent, that the case is not brought before the court. The Contested Provision hampers implementation of such requirement in State administration.

The Ombudsman concludes that the Contested Provision creates preconditions for restriction of the basic rights of persons that are not proportionate with the objective set and moreover it also restrict implementation of the principle of justice and the principle of good administration.

The Constitutional Court holds:

6. The first part of Section 33.1 of the Tax Law came into force on May 17, 2000 and was effective up to May 1, 2004. At the moment of submission of the application, on October 4, 2007, the abovementioned provision has not been effective for more than three years already.

Observing efficiency of the Constitutional Court procedure, it is necessary into account the fact that this judgment in such cases shall be significant only if it will be determined an antedate force. Consequently, legal proceedings in such cases are possible if the legal relations to be assessed allow assigning antedate to the judgment of the Constitutional Court. However, if cancelling of the Contested Provision from the date of passing or coming into force thereof could cause, for instance, a considerable violation or threat of the State (society) interests, then usefulness of continuing legal proceedings shall be assessed during preparation of the decision of the Constitutional Court.

7. In the application, it has been asked to assess compliance of the Contested Provision with Article 1 pf the Satversme, namely, with the principle of proportionality that follows from this Article, because the Applicant regards the Contested Provision as non-compliant with this principle in particular.

Several principles of a law governed state, including the principle of proportionality, follow from the notion of a democratic republic included in Article 1 of the Satversme. [*see: Judgment of March 24, 2000 by the Constitutional Court in the case No. 04-07(99), Para 3 of the Concluding Part*]. The principle of proportionality means that if the public power restricts the rights or a person and his or her legal interests, it is necessary to ensure a reasonable balance between the interests of a persons and the State or that of the society (*see, for instance: Judgment of March 19, 2002 by the Constitutional Court in the case No. 2001-12-01, Para 3.1 of the Concluding Part and Judgment of March 25, 2003 by the Constitutional Court in the case No. 2002-12-01, Para 5 of the Concluding Part*).

When assessing compliance of the Contested Provision with the principle of proportionality, it is also necessary to take into consideration the fact that manifestation of the abovementioned principle in different fields of law may differ. The nature of the contested provision, inter alia, also its connection with other norms of the Satversme and their place in the system of fundamental rights, inevitably influence the scope of the control, realized by the Constitutional Court. Namely, the freedom of action of the legislator, when regulating the particular issue, may be broader or narrower, and the Constitutional Court must assess whether the scope of freedom of action used by the Saeima complies to what has been established in the Satversme (*see: Judgment of*

November 8, 2006 by the Constitutional Court in the case No. 2006-04-01, Para 15.2 and 15.3).

In the tax law, like in other fields of law, the State is obligated to observe, to protect and ensure the rights of a person. For the State to act in accordance with the human rights, it has to implement a range of measures – both, passive, for instance, non-interference with the rights of a person, and active, for instance ensuring of meeting individual needs of a person (*see: Koch I.E., Dichotomies, Trichotomies or Waves of Duties? Human Rights Law Review, 2005, Vol. 5, Number 1, pp. 82 – 86*).

Consequently, also in the field of tax law, the State has different responsibilities. Namely, its freedom of action and consequently the limits of constitutional control regarding the order of determination of the amount of taxes and the order, according to which fines for unpaid taxes are collected, may differ. The State is obligated to form an effective tax system in the interest of welfare of the society. However, the State also is obligated to protect persons from non-proportionate fines even if they are imposed for violation of tax laws.

The Constitutional Court has also recognized in its practice that the State is obligated to establish responsibility of paying taxes and this responsibility *per se* does not violate the basic rights of a person. However, the duty to pay taxes is closely related to establishment of the measures for fulfilment of this responsibility, namely, the State not only obligates taxpayers to pay taxes of a certain amount, but it also provides for the order of assessment, withholding and payment of taxes, as well as the liability for non-fulfilment of this duty.

Proper tax administration includes timely and efficient tax collection and at the same time prevents tax evasion. Tax payment is the responsibility of both – legal persons and natural persons. The tax rate of each tax payer is established by law. The duty of paying taxes always entails restrictions of property rights, as well as can be related to other restrictions established by law, which must be proportionate to the legitimate objective – protection of values of constitutional importance.

The Legislator has a considerable freedom of action in establishing the tax control and procedure thereof. It means that the Legislator is entitled at own discretion, observing the principle of proportionality, to establish the procedure and terms of tax assessment, withholding, and payment, as well as the rights, responsibilities, and

liability of the tax payers and the tax administration (*see: Judgment of April 11, 2007 by the Constitutional Court in the case No. 2006-28-01, Para 13 and 19.1*).

8. It is also necessary to take into consideration that interaction of the national norm of human rights in the system of the Satversme and the international legal norms is regulated by Article 89 of the Satversme, which establishes: "The State shall recognize and protect fundamental human rights in accordance with this Constitution, laws and international agreements binding upon Latvia". From this Article it can be seen that the aim of the legislator has not been to oppose the norms on human rights, incorporated in the Satversme to the international norms of human rights, quite to the contrary – it has been to reach mutual harmony of the norms (*see: Judgment of June 27, 2003 by the Constitutional Court in the case No. 2003–04–01, Para 1 of the Concluding Part and Judgment of January 17, 2005 by the Constitutional Court in the case No. 2004–10–01, Para 7.1*). Thus, when interpreting the Satversme and international liabilities of Latvia, one should look for the interpretation, which ensures harmony, but not confronting (*see: Judgment of August 30, 2000 by the Constitutional Court in the case No. 2000-03-01, Para 5 of the Concluding Part and Judgment of May 13, 2005 by the Constitutional Court in the case No. 04-18-0106, Para 5 of the Concluding Part*).

Consequently, international law and the practice of application thereof may serve as means for clarifying the content of the legal norms and principles included in the Satversme.

The European Court of Human Rights, when assessing tax issues, has concluded that a state enjoys a considerable freedom of action in the field of taxes (*see, e.g.: Judgment of the ECHR in the cases: Gasus Dosier- und Fördertechnik GmbH v. the Netherlands, judgement of 23 February 1995, Series A no. 306-B, para. 60; Jokela v. Finland, judgement of 21 May 2002, Para. 57; Burden and Burden v. the United Kingdom, judgement of 12 December 2006, Para. 54*). Moreover, a state is entitled to adopt all necessary laws in order to ensure tax payment (*see, e.g.: Judgment of the ECHR in the cases: Gasus Dosier- und Fördertechnik GmbH v. the Netherlands, judgment of 23 February 1995, Series A no. 306-B, Para. 59; Mamidakis c. Greece, arrêt du 11 janvier 2007, n^{o} 35533/04, Para. 48*).

9. Constitutional courts of other states have also recognized that in the field of taxes a state enjoys a considerable freedom of action. For instance, the Constitutional Court of

Belgium has recognized that the legislator enjoys a broad freedom of action when determining taxes, however the tax may not be non-proportionate and ungrounded in relation to property, and it must ensure a reasonable balance between the interests of the society and the rights of a person to property. The legislator is also entitled to provide for strict measures in order to impact activities of a taxpayer (*see: Arrêt n^{0} 107/2005 du 22 juin 2005 de la Cour constitutionnelle de Belgique, para 15.2 et 15.4, http://www.const-court.be*).

The Constitutional Court of Lithuania has also recognized that Although under the Constitution the Seimas is granted competence to establish state taxes, as well as legal responsibility for violations of tax laws, however, it does not mean that the legislator may establish any type of legal responsibility or any type of penalties or fines of any size for violations of tax laws (*see:. Chapter 2 Clause 6 of the concluding part in the Judgment of Lithuanian Constitutional Court of 6 December 2002 in Case No. 6/99-23/99-5/2000-8/2000, http://www.lrkt.lt/dokumentai/2000/r001206.htm)*.

10. The Applicant, when assessing the rights to cancel the fine imposed by the SRS, has also recognized that imposing of a fine as a mandatory administrative act shall be cancelled only in the cases when the Court established that the essence and the nature of the violation is of the kind that the maximum penalty would be non-proportionate (*see, e.g.: Judgment of September 26, 2006 by the Department of Administrative Cases of the Supreme Court of the Republic of Latvia, Para 7. Case materials, Vol. 2, pp. 15*).

11. The Contested Provision is related to the field of taxes, however it provides for preconditions (restrictions) for reducing a fine. Whilst, legal norms that regulate responsibility for violation of tax laws are at large extent related to that field of activities of the State, wherein the State implements the function of inflict penalty. On the one hand, the legislator must ensure an effective area of regulation for protection of the basic rights in this field because different principles are effective in the normative regulation of the tax system and the fine system. By means of the tax rights, the State acquires the resources necessary for implementation of its functions, whilst the fine system ensures appropriate observance of other rights. Consequently, imposing of a fine shall be possible only within the limits of necessity and so far as it ensures an appropriate observance of other legal regulation.

However, on the other hand, legal regulation that provides for responsibility for violation of tax laws also must be efficient. Legal regulation of tax laws as such would not be sufficient if no effective system of violation prevention would exist. Efficiency of the abovementioned system is guaranteed by both, inevitability of fine and severity of punishment, unless it is proportionate with the violation or the "benefit" gained in the result of it. However, in this field, too, the duty of the State is to ensure individualization of a fine as far as it is allowed by the specific character of the controllable relations, namely, to make it adequate to the violation committed.

Consequently, the legislator enjoys a broad freedom of action within the limits of normative regulation of taxes. However, fines for tax law violations may not be apparently non-proportionate with the objective that the legislator has planned to achieve.

12. The Contested Provision established an imperative claim that denies rights to the SRS and the administrative courts to assess proportionality of fines, namely, to reduce the fine imposed more often than once per three years. In fact, the Contested Provision denies rights to a taxpayer to ask to find a possibility individually assess the possibility to reduce fine imposed. The Saeima, in its reply, also regards the Contested Provision as a prohibition, namely, as a provision that restricts reducing of a fine and that be related to approaches of tax policy established in the Tax Law.

Consequently, the prohibition established in the Contested Provision shall be regarded as a restriction.

13. When assessing whether the restriction included in the Contested Provision complies with Article 1 of the Satversme, it is necessary to establish:

1) whether the restriction has been established by law;

2) whether the restriction has a legitimate objective;

3) whether the restriction is proportionate with the legitimate objective.

14. The Contested Provision that provides for the rights of the tax administration to assess the possibility to reduce the fine imposed not more often than once per three years has been established according to a law passed in an adequate order. Namely, the Contested

Provision is included in the Tax Law that has been adopted and announced according to the order established in the Satversme and the Saeima Rules of Order.

Consequently, the Contested Provision has been established by law.

15. In the basis of each restriction of rights must contain circumstances and arguments why it has been necessary. A restriction needs a legitimate objective, namely, it must be established for protection of substantial interests of the society.

When establishing restriction of human basic rights, the responsibility to present and justify the legitimate objective of such restrictions, during the proceedings of the Constitutional Court, falls upon the institution, which has passed the contested provision – the Saeima. However it was not indicated in the answer of the Saeima what is the legitimate objective of the provision of the Law On Personal Income Tax, in accordance to which pensions are included into the list of incomes chargeable with the personal income tax, and the responsibility of the Constitutional Court *ex officio* is to assess objectively all circumstances of the case and state presence or, on contrary, absence of such legitimate objective (*see: Judgment of June 8, 2007 by the Constitutional Court in the case No. 2007-01-01, Para 23*).

It can be concluded from the application that the Applicant does not contest the legitimate objective of the Contested Provision. However, it follows from what has been indicated in the reply of the Saeima that the objective of the Contested Provision is to favour honesty of taxpayers. Such norm allows reducing the fine imposed one per three years if the person has not acted ill-intentionally, as well as it simultaneously prohibits reducing the fine if the taxpayer has violated laws repeatedly or systematically. Consequently, it is possible to conclude that the legitimate objective of the first part of Section 33.1 of the Tax Law is related to the intention of the Saeima to make imposing fines more individual. Namely, it provides for a possibility to assess the action of the violator taking into account what has been established in the norm.

The Constitutional Court has recognizes that The basic function of the personal income tax as a direct tax is the fiscal function, which ensures incomes in the national budget and municipal budgets. With the help of these incomes it is possible to fund prior social and economic activities, as well as to decrease inequality of the level of persons' incomes and welfare (*see: Judgment of June 8, 2007 by the Constitutional*

Court in the case No. 2007-01-01, Para 23). Simultaneously, tax laws fulfil an economic (regulatory) function, namely, it equalizes the interests of the State and those of taxpayers, as well as impacts the action of taxpayers.

On the other hand, the norms that provide for responsibility for violation of tax laws favour adequate and timely tax payment, and in a broader sense – it impacts the action of taxpayers. The ECHR also recognizes prevention of tax evasion as a legitimate objective (*see: Hentrich v. France, judgment of 22 September 1994, Series A no. 296-A, pp. 19-20, Para. 39*).

Consequently, it is possible to conclude that the legal norms that provide for responsibility for violation of tax laws or preconditions for releasing form this responsibility have been established in favour of the interests of the society.

Consequently, the Contested Provision has a legitimate objective.

16. In order to find out whether the restriction is proportionate with the legitimate objective that the State has planned to achieve by establishing this restriction, it is necessary to assess whether a reasonable balance between the interests of the State and that of the society is ensured. The Contested Provision must ensure balance between the rights of the State to provide for responsibility for violation of tax law on the one hand and the rights of taxpayers to as the SRS and an administrative court to assess whether a fine proportionate with the essence and nature of the violation committed has been applied to him or her on the other.

In order to assess whether the restriction included in the legal norm adopted by the legislator complies with the principle of proportionality, it is necessary to find out:

first of all, if the means, used by the legislator are suitable for achieving the legitimate objective;

secondly, if such an activity is required, i.e., if it is not possible to attain the objective by other means, which would less limit the rights and legal interests of an individual;

thirdly, if the activity of the legislator is proportionate or adequate, i.e., if the benefit, obtained by the society, is greater than the loss incurred to the rights and lawful interests of an individual.

If, after evaluating the legal norm, it is acknowledged that it does not comply with even one of the above criteria, then it shall be considered as not being in conformity with the principle of proportionality and illegitimate (*see: Judgment of March 19, 2002 by the Constitutional Court in the case No. 2001-12-01, Para 3.1 of the Concluding Part*).

16.1. The means selected by the legislator are appropriate for reaching the legitimate objective, if this objective was reached by means of the particular regulation.

The Constitutional Court holds that it is not possible to assess the Contested Provision taken separately from the first part of Section 33.1 of the Tax Law that it pertains to. Consequently, it is necessary to establish whey the Tax Law was supplemented by Section 33.1 on April 2000.

It follows from the case materials that the draft law was submitted to the Saeima by the Cabinet of Ministers (*see: case materials, Vol. 1, pp. 167 and 168*). However the draft law did not initially contain the contested provision – it was included therein only in the third reading (*see: http://www.saeima.lv/saeima7/reg.likprj).*

Up to the moment when the Contested Provision came into force, the responsibility for reduction of tax amount was basically regulated by Section 32 of the Tax Law. This norm provided that in the case if

If a taxpayer in violating the requirements of tax laws, the tax administration shall assess and recover for the benefit of the budget from the taxpayer the reduced tax amount and a fine to the amount of such. Hence, the abovementioned legal norm imperatively provided that reducing of the tax amount is finable at the amount of 100 percent from the unpaid (missing) part of the tax. This meant that the responsibility of a taxpayer for reducing the tax amount set in disregarding the fact whether the taxpayer has caused real damage to the State budget by means of such activity and whether the violation has been committed on purpose or accidentally. The tax administration had no reason to assess these circumstances and it was neither entitled to take them into consideration when establishing the amount of a fine.

By means of Section 33.1 of the Tax Law, a mechanism has been created, which allowed to reduce the amount of the fine imposed by assessing the essence and nature of the violation committed by the a taxpayer. Consequently, the first part of Section 33.1 of the Tax Law includes a possibility to make a more lenient and individually assessed decision in

the cases when the decision of the tax administration, wherewith the fine was imposed, could be appealed against.

However, the Contested Provision as a part of Section 33.1 of the Tax Law provided for preconditions for reducing the amount of the fine. By emphasizing favouring of honesty of taxpayers, it did not permit a possibility to reduce the amount of a fine more often than once per three years after having assessed the situation. Taking into consideration the fact that before adoption of the first part of Section 33.1 of the Tax Law no reducing of a fine was possible, adoption of the abovementioned norm can be regarded as a considerable step away from the general prohibition to assess the essence and nature of a violation.

The first part of Section 33.1 of the Tax Law is appropriate for reaching the legitimate objective, namely, it provides the SRS and courts with a possibility to assess the essence and nature of the violation committed by a taxpayer according to the order and extent established in the Contested Provision, as well as to assess proportionality of the fine imposed.

16.2. The restriction of fundamental rights determined in the impugned norm is proportionate only if there are no other means, which are as effectual and by choosing them the fundamental rights will be restricted in a lesser degree. When assessing whether the legitimate aim may be reached in a more lenient way, the Constitutional Court takes into consideration that a more lenient means are not any means, but only such by which the aim may be reached in the same quality (*see: Judgment of May 13, 2005 by the Constitutional Court in the case No. 2004–18–0106, Para 19*).

It can be concluded form the wording of the first part of Section 33.1 of the Tax Law, which came into force on May 1, 2004, that the legislator has established and provided for such regulation that allows reaching the legitimate objective using other mans that restrict the rights and legal interests of a person at a lesser extent. Namely, the abovementioned norm provided that the tax administration in evaluating the essence and nature of the violation of the taxpayer, the fact of how many times the violation has been committed, the harm caused and the integrity of the taxpayer in cases where the taxpayer has disputed the decision of the tax administration, has the right to reduce the fine imposed as a result of controls up to 70 per cent of the amount, but not more often than once a year.

Consequently, the legislator has passed a norm that restricted the rights and legal interests of a person at a lesser extent, and that conferred the tax administration the right to weigh the possibility to reduce the fine imposed more often.

As it is indicated by the Saeima, the Contested Provision systematically was related to the first part of Section 23 of the Tax law, which provided that the tax administration has the right, after a tax review (audit), to adjust the amount of taxes and to impose fines within a period of three years after the payment time period specified by law if regulations regarding fees and taxes have been violated. Moreover, in this period of time audits were planned and carried out for taxpayers once per three years. Based on the abovementioned, the Saeima holds that it was not necessary to systematically provide for the possibility to reduce the fine imposed more often than once per three years.

After having got acquainted with the area of regulation of the Tax Law, it can be concluded that it was permitted to carry out tax reviews (audits) more often than once per three years. The three years established in the first part of Section 23 of the Tax Law that the Saeima refers to provide not for the frequency of reviews (audits), but for the period, after the expiry of which the SRS has no more right to carry out the abovementioned activities. For instance, according to Item 11 of Section 8 of the Law "On State Revenue Service", the SRS was obligated to carry out tax calculation and tax reviews (audits) for enterprises (companies) on request of pre-trial investigation institutions and a court. It was also possible that audits on several kinds of taxes have been carried out during the period of tree years for a taxpayer.

The abovementioned is also confirmed by the SRS by indicating that the issue of reducing the amount of the fine was assessed based on a request of taxpayers in order to ensure a possibility to reduce the fine imposes as the result of controls for violations established in further controls (*see: case materials, Vol. 2, pp. 9*). Namely, the SRS admits that the basis for reducing a fine has been a request of the taxpayer, because several reviews have been carried out during the period of three years, and therefore several fines have been imposed.

Consequently, the aforesaid does not makes one conclude that only one tax review or audit is possible for one and the same taxpayer during the period of three years. Similarly, a fine could be imposed on a taxpayer more often than once per three years.

It also follows from the case materials that the first part of Section 33.1 of the Tax Law was once applied to the applicant to the administrative court – the limited liability company "Baltic Feed" – on July 5, 2001 by the Decree No. 19/12354 of the SRS [*see: Judgment of March 19, 2007 by the Administrative Regional Court in the case No. A42030004 (AA43-0052-07/14), Para 16.5. Case materials, Vol. 1, pp. 205*]. Nevertheless, already on October 7, 2003, the deputy director of the Zemgale Regional Department of the SRS passed Resolution No. 12.01-29/222 regarding the same persons by thus additionally providing for the custom duty and a fine, as well as the value added tax and a fine and the natural resources tax and a fine at the amount of 200 percent to be paid into the budget [*see: Judgment of March 19, 2007 by the Administrative Regional Court in the case No. A42030004 (AA43-0052-07/14), Para 1. Case materials, Vol. 1, pp. 197 and 198*].

Consequently it is possible to conclude that a fine for tax violations could be imposed on one and the same persons more often than once per three years. However, the right of the SRS to decide on reducing of a fine, as well as the right of the administrative court to assess proportionality of the fine imposed by the SRS were restricted. Namely, the rights could not be exercised more often than once per three years.

If the Contested Provision was eliminated from the first part of Section 33.1 of the Tax Law, the SRS would have the right to assess the essence and nature of the violation committed and to reduce the fine imposed. This would ensure individualization of fining.

Consequently, the legitimate objective of the Contested Provision could be reached by other means that would restrict the rights of a person at a lesser extent.

16.3. When assessing whether the action of the legislator has been adequate, i.e. whether the benefit that is gained by the society is greater that the harm done to the rights and legal interests of a person, it is necessary to take into consideration the fact that it often happens in practice that a taxpayer may not be regarded as an ill-intentioned nonpayer, but he or she has rather made a mistake by, for instance, including the pre-tax in the declaration two days earlier than he or she should, which should be done only the following month (*see: Judgment of March 30, 2005 by the Administrative Case Department of the Supreme Court of the Republic of Latvia in the case No. SKA-21. Latvijas Republikas Augstākās tiesas Senāta Administratīvo lietu departamenta spriedumi un lēmumi 2005. – Rīga: Tiesu namu aģentūra, 2006, pp. 50 – 57*). Hence the Contested Provision is equally related to

both, those cases when the essence and nature of violation makes one think of malevolence (conscious action) and those cases when no such malevolence can be established.

The Constitutional Court holds that the task of the legislator, when deciding on punishment, is to achieve individualization of legal regulation at the greater extent possible. However, individualization of legal regulation may also have its own limits that is determined (influenced) by, for instance, requirements of the field of law. Namely, the legislator, when assessing all conditions of the particular field (branch), has the right to establish regulation that would not ensure an absolute individualization of legal regulation and is equally applicable to comparable, however different cases.

The benefit that the society gains from the existence of the Contested Provision is payment of a fine at full extent without considering the possibility to reduce it. Hence, this benefit is additional income into the State budget.

When assessing the harm dome to persons, it is necessary to take into consideration the fact that each restriction of rights must be analysed in the context of a particular case, however it must be done based on the principle of proportionality. In this case it is necessary to assess at what extent protection of the interests of the State is necessary in the field of tax collection in order to ensure welfare of the society. Namely, it is important to balance the rights of separate persons to assessment of an individual violation with the duty of the State to ensure an efficient tax administration system.

In the case under review, these interests may not be recognized as balanced. The Contested Provision is related to all persons who have committed a repeated violation of tax laws within the period of three years. In this situation there were no mechanism that would allow assessing individual circumstances in the case of a repeated violation and to decide on the possibility to reduce the fine imposed. Consequently, in separate cases, a person, even if it has not been recognized as an ill-intentioned nonpayer of taxes, could be punished by means of a fine inadequate to the violation. Moreover, the prohibition included in the Contested Provision existed disregarding the amount of the fine imposed and the ability of the person to pay the fine imposed, as well as the consequences that set in for a natural person in the case of non-payment of taxes, for example, possible insolvency. It is also necessary to take into consideration the fact that a fine as such is inadmissible if it basically serves as means for obtaining additional income into the State budget.

Consequently, the harm done by the Contested Provision to the rights and legal interests of persons is greater than the benefit that the society gains from existence of this norm.

Since it is possible to reach the legitimate objective by mans of more lenient means and the harm done by this norm to the rights and legal interests of persons is greater than the benefit gained by the society, it shall be regarded as non-compliant with the principle of proportionality and also with Article 1 of the Satversme.

17. The Applicant asked in the application to recognize the words "not more often than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004) as non-compliant with Article 1 of the Satversme and invalid from the day of passing thereof. Although there was no case initiated regarding compliance of this norm with a legal norm (act) of a higher legal force, it is possible to conclude that this case includes a regulation similar to the Contested Provision. Namely, the words "not more often than once per three years" also provides for a restriction that prohibits the SRS and administrative courts to decide on reducing of a fine more often than it is provided in the norm. This norm, like the Contested Provision, did not allow the tax administration to individually assess the essence and nature of the violation in the case of a repeated commitment thereof.

On the one hand, it could be possible to conclude that no reply of the Saeima has been received regarding compliance of the words "not more than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004) with Article 1 of the Satversme, and hence the Constitutional Court does not have the right to assess compliance of this norm with a legal norm (act) of a higher legal force. However, on the other hand, it is evident that this norm was closely related with the Contested Provision and in fact substituted it. The abovementioned words also provided for a restriction analogous to the one that was recognized by the Constitutional Court as non-compliant with Article 1 of the Satversme. Namely, these words restricted the possibility to assess proportionality of the fine imposed by means of a limited term – one year in this case.

It is asked in the application to recognize the words "not more often than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004) as non-compliant with Article 1 of the Satversme, and the request of the Applicant is significant in relation to establishment of the limits of the claim in the Constitutional Court procedure.

Namely, in the case of doubt, what has been indicated in the application can very well reveal the objective that the Applicant has wanted to reach by submitting an application to the Constitutional Court.

It follows from the principle of procedural economy that it would not be useful to repeatedly decide on the issues that could be adjudicated in the case under review. The Constitutional Court has concluded that "exceeding the limits of the claim in a judgment is permitted and even necessary in order to ensure a more efficient protection of rights of a person and execution of a judgment" (*see: Judgment of December 19, 2007 by the Constitutional Court in the case No. 2007–13–03, Para 6 and Judgment of January 17, 2008 by the Constitutional Court in the case No. 2007–11–03, Para 18*). It has also been expressed in law that, in the Constitutional Court procedure "there can be cases when it is admissible and even necessary to exceed the limits of the claim by including also such norms in investigation that have not been contested or by assessing compliance of those norms, compliance of which has not been contested" (*Endziņš A. Kā vērtēt jaunāko Satversmes tiesas praksi // Jurista Vārds, October, 9, 2007, No. 41, pp.* 5).

Broadening of the limits of the claim may take place in cases when it is required by observation of the principles of the Constitutional Court procedure. Simultaneously it is necessary to take into consideration the fact that the Constitutional Court may broaden the *ex officio* limits of the claim only by observing certain criteria, first of all "conception of close relation".

In order to conclude whether it is possible and necessary to *ex officio* broaden the limits of the claim in relation to other norms, it is necessary to investigate:

1) whether those norms, in relation to which the claim is being *ex officio* broadened, are so closely related to the contested norms expressis verbis contested in the case under review that assessment of them is possible in the frameworks of the same justification or necessary for adjudication of the case under review;

2) whether broadening of the limits of the claim is necessary for observation of the Constitutional Court procedure.

The Contested provision and the words "not more often than once per year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004) were adopted based on one and the same understanding of the legislator regarding its freedom of action in the

field of tax rights. Therefore recognition of both these norms as non-compliant with Section1 of the Satversme is possible in the frameworks of the same justification.

In this case, the Constitutional Court in fact has investigated compliance of the viewpoints of the legislator with legal norms of higher legal force, based on which the Saeima has passed not only the Contested Provision, but also the words "not more often than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004). Consequently, the Constitutional Court has in fact adjudicated the legal dispute regarding compliance of these norms with the Satversme.

The task of the Constitutional Court is to settle disputes that arise regarding compliance of acts of a lower legal force with the legal norms of a higher legal force (*see: Judgment of February 22, 2002 by the Constitutional Court in the case No. 2001-06-03, Para 2.2 of the Concluding Part and Judgment of October 18, 2007 by the Constitutional Court in the case No. 2007-03-01, Para 9*). Item 4 of the fifth part of Article 20 of the Constitutional Court law prohibits initiating a case in the Constitutional Court regarding an already reviewed claim, whereas Item 5 of the first part of Article 29 of the Constitutional Court Law provides that proceedings in the case may be closed if "a judgment in another case on the same claim subject has been announced". Item 2 and 4 of the first part of Article 29 of the Constitutional Court Law "is directed towards ensuring of economy of the Constitutional Court procedure and ensuring that the Constitutional Court should not prepare a judgment in cases where there is no dispute. If there is no dispute, the procedure of the Constitutional Court is senseless" (*see: Judgment of June 12, 2007 by the Constitutional Court in the case No. 2007-06-03, Para 11.2*).

Consequently, it is possible to recognize the words "not more often than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004) as non-compliant with the principle of proportionality.

18. The Saeima indicates that recognition of the Contested Provision as invalid would not solve all problems, because the judgment of the Constitutional Court would in fact require a positive regulation of the legislator and, most probably, revision of other norms effective at that time. However, the Applicant indicates that in the case of deleting of the Contested Provision no positive regulation would be possible. Namely, the cases, in which the contested provisions have been previously applied by an institution, could be

adjudicated by observing the essence and nature of the violation and by directly applying the principle of proportionality.

The Constitutional Court reminds that the basic task is not to decide who in each particular case legal norms should be applied (*see: Judgment of January 4, 2005 by the Constitutional Court in the case No. 2004–16–01, Para 17*). Questions related to application and interpretation of certain legal norms generally fall within the scope of responsibility of the courts of general jurisdiction and administrative courts. Hence, the Constitutional Court has no grounds for contesting what has been indicated by the Applicant that it is possible to recognize the Contested Provision as invalid without making additional amendments to laws.

19. Since the Constitutional Court has recognized the words "not more often than once a year" of the first part of Section 33.1 (wording of March 31, 2004) as non-compliant with Article 1 of the Satversme, it is necessary to decide on the issue regarding the date when the abovementioned norms would become invalid.

The Applicant has asked to recognize the Contested Provision as invalid from the date of passing thereof. However, this issue has not been analysed in the reply of the Saeima.

The Constitutional Court has already recognized that in the cases, wherein compliance of an invalid legal norm with legal norms of a higher legal power is being assessed, it is possible to determine an antedate force for a judgment (*see: Para 6 of this Judgment*). As to the Contested Provision, the Constitutional Court recognizes that it is not possible to objectively determine any other date, from which it could be announced as invalid, but the date indicated in the application, namely, the date of passing of the Contested Provision.

The abovementioned conclusion can be applied also to the words "not more often than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004). Namely, the Applicant has asked to recognize the contested norms as invalid from the date of passing thereof, and the Constitutional Court does not see any other objectively determined date but the date of passing of the norm.

20. The Constitutional Court also takes into consideration the fact that deleting of the Contested Provision from the date of passing thereof may not cause substantial invasion or threat to the interests of the State (society) (*see, e.g.: Judgment of December 16, 2005 by the Constitutional Court in the case No. 2005-12-0103, Para 25*). Since the field of taxes is an important field of the activities of the State, no such situation would be admissible when cancelling of the Contested Provision would lead to revision of those decisions of the SRS, which have became effective and to which this norm could be applied.

Consequently, the Constitutional Court holds that in this case cancelling of the Contested Provision and the words "not more often than once a year" of the first part of Section 33.1 of the Tax Law (wording of March 31, 2004) could be assign an antedate force. An appropriate solution for this situation is cancelling of the abovementioned norms in relation to the things that still undergo proceedings. Namely, to the things, wherein persons have contested and appealed against fines imposed by the SRS or recalculated taxes and the final decisions have not jet become effective before coming into force of this Judgment.

The Substantive Part

Under Articles 30 – 32 of the Constitutional Court Law, the Constitutional Court

holds:

1. In relation to the cases undergoing proceedings, the words "not more often than once per three years" of the first part of Section 33.1 of the Law "On Taxes and Fees" (wording of April 13, 2000) do not comply with Article 1 of the Satversme of the Republic of Latvia and invalid from the date of passing thereof.

2. In relation to the cases undergoing proceedings, the words "not more often than once a year" of the first part of Section 33.1 of the Law "On Taxes and Fees" (wording of

March 31, 2004) do not comply with Article 1 of the Satversme of the Republic of Latvia and invalid form the date of passing thereof.

The Judgment is final and not subject to appeal.

The Judgment takes effect as of the day of publishing it.

The Presiding Judge G. Kūtris