



Satversmes tiesa

Press Release

Case No 2020-31-01

7 April 2021

The Constitutional Court adopts a judgment in the case concerning the constitutionality of the provision which imposes a penalty of a fixed amount for a failure to fulfil certain taxpayer obligations

On 6 April 2021, the Constitutional Court passed a judgment in Case No 2020-31-01 "On the compliance of Section 34(1) of the law 'On Taxes and Duties', insofar as it envisages calculation and collection from the taxpayer of a fine in the amount of 100 percent of the underpaid tax due to the budget, with Article 105 of the Constitution of the Republic of Latvia".

CONTESTED PROVISIONS

- Section 34(1) of the law "On Taxes and Duties" (hereinafter – the contested provision):

"If a natural or legal person who is registered as a performer of economic activity engages in economic activity without registering as a payer of a particular tax or, within 30 days after the deadline set by the tax authority, does not submit the tax declarations provided for by tax laws, as well as business and accounting records requested by the tax authority without which the tax administration officers (employees) are unable to determine the amount of the tax liability, then the tax authority shall, on the basis of a tax review (audit), calculate and recover from the taxpayer for the benefit of the budget the tax calculated for the taxation period starting from the date on which the person had an obligation to register as a taxpayer, a late payment charge in the amount provided for in Section 29(2) of this Law, and a fine in the amount of 100 percent of the tax payable to the budget."

PROVISION OF SUPERIOR LEGAL FORCE

- Article 105 of the Constitution (Satversme) of the Republic of Latvia (hereinafter – the Constitution):

"Everyone has the right to own property. Property shall not be used contrary to the interests of the public. Property rights may be restricted only in accordance with law. Expropriation of property for public purposes shall be

allowed only in exceptional cases on the basis of a specific law and in return for fair compensation.”

FACTS OF THE CASE

The case was initiated on the basis of an application by Jānis Pīlāts. The State Revenue Service had carried out a tax audit in respect of the Applicant, which resulted in additional tax payments due. Also, pursuant to the contested provision, a fine linked to the tax payments was calculated in the amount of 100%. The Applicant appealed the respective decision in the administrative court; however, in the part concerning the fine, the decision was left unchanged.

The Applicant notes that the contested provision does not envisage the possibility for the party applying the law to choose the most appropriate amount of fine on case-by-case basis. Allegedly, such restriction of rights is disproportionate. Thus, the Applicant’s right to property, as guaranteed by Article 105 of the Constitution, is infringed on.

THE COURT’S FINDINGS

Clarifying the claim

The Constitutional Court determined that it would evaluate the compliance of the contested provision with Article 105 of the Constitution in respect of all the taxpayers falling within the scope of the contested provision, regardless of the types of violations referred to in the contested provision and of whether the violator is a natural or legal person. [12]

On the scope of Article 105 of the Constitution and on the restriction of the taxpayer’s fundamental rights

The Constitutional Court concluded that the contested provision does not concern expropriation of property for public purposes and that its constitutionality should be evaluated under the scope of the first three sentences of Article 105 of the Constitution. [13.1]

The Constitutional Court noted: since the obligation to pay a financial penalty always infringes on the individual’s right to property, the obligation imposed by the contested provision – to pay the fine stipulated in it – infringes on the taxpayer’s property, more specifically, diminishes its amount. [13.2]

On whether the restriction of fundamental rights imposed by the contested provision was established by law and has a legitimate aim

The Constitutional Court found that the restriction of fundamental rights contained in the contested provision was established by a law, which had been adopted following proper procedure. [15]

Also, the Constitutional Court concluded that this restriction has legitimate aims – to protect public welfare and the democratic structure of the state. Furthermore, the Constitutional Court reminded that ensuring tax revenues is directly linked to the individual's constitutional obligations to the Latvian State. Such obligations are targeted at a sustainable implementation of the sovereign's will – to live in a democratic rule-of-law state – enshrined in the basic norm of the State of Latvia. Failure to fulfil such obligations threatens the existence of every democratic rule-of-law state. [16]

On the appropriate way of evaluating whether the restriction of fundamental rights imposed by the contested provision complies with the principle of proportionality

The Constitutional Court noted that the fine provided for in the contested provision is applicable in two situations: firstly, in the event of a violation of the obligation to register, i.e., performing economic activity without registering as a payer of a particular tax if the individual is registered as a performer of economic activity, and, secondly, in the event of a violation of the obligation to present documents, namely, a failure to duly submit the declarations specified in tax laws, as well as the documents necessary for calculating the amount of tax payable. The legal nature of these obligations differs, therefore, in examining whether the restriction of fundamental rights imposed by the contested provision complies with the principle of proportionality, the Constitutional Court evaluated the means selected by the legislator with reference to each of the violations provided for in the contested provision. [17]

On whether the means selected by the legislator are appropriate for achieving the legitimate aim

The Constitutional Court concluded that the means chosen by the legislator are appropriate for achieving the legitimate aim of the restriction of fundamental rights contained in the contested provision. In fulfilling its obligation to ensure state budget receives revenues from taxes, and in determining the policy of tax penalties, the legislator enjoys certain discretion. One of the aspects of such discretion is the possibility to provide for punitive measures to impact the taxpayer's behaviour and thus ensure that tax revenues are received. The fine provided for in the contested provision is to be considered as such a punitive measure. Thus, the restriction of fundamental rights imposed by the contested provision contributes to the protection of public welfare and the democratic structure of the State both when the obligation to register is violated and when the obligation to present documents is violated. [18.3]

On whether the means selected by the legislator are necessary for achieving the legitimate aim

The Constitutional Court had to examine whether individualisation of the fine provided for in the contested provision is necessary in cases of violation of the obligation to register and violation of the obligation to present documents depending on the character of the violation. [19]

The Constitutional Court found that, in the case of a violation of the obligation to register, individualisation of the amount of fine is necessary as such a violation may take different forms. Namely, there can be situations where this violation is due to ignorance or inadvertence, as well as situations where it is committed knowingly in bad faith and is related to tax evasion. Having found that the individualisation of the amount of fine in the case of a violation of the obligation to register would not demand investment of excessive state or public resources, the Constitutional Court concluded that, as far as the violation of the obligation to register is concerned, the legitimate aims of the restriction of fundamental rights imposed by the contested provision can be achieved by less restrictive means. [20.1, 20.2]

Conversely, in the case of a violation of the obligation to present documents, individualisation of the amount of fine is not necessary as, in a typical situation, it is indicative of the taxpayer's deliberate action to evade taxes. Therefore, in the case of a violation of the obligation to present documents, no other, more lenient, means exist which would allow to achieve the legitimate aims of the restriction of fundamental rights imposed by the contested provision at least at the same quality level. [21]

On whether the restriction of the taxpayer's fundamental rights outweighs the benefit for society

The Constitutional Court noted: to state that the adverse consequences arising for the taxpayer as a result of restriction of their fundamental rights do not outweigh the benefit gained from this restriction by the whole of society, it is necessary to examine whether the fine provided for in the contested provision, applied in case of a violation of the obligation to present documents, is effective and dissuasive. [22.1]

The Constitutional Court assessed the tax-paying culture in Latvia and found that, since the transformation of the Latvian legal system began, the poor-quality legal framework for taxes and its formalistic, mechanical application have reduced taxpayers' confidence in the State and law, tax administration in particular. The Constitutional Court also noted that the level of shadow economy in Latvia is still high, while the understanding about an individual's constitutional obligation to pay taxes is still insufficient. Therefore, the fine in the amount of

100 percent of the tax payable to the budget, applied pursuant to the contested provision without an individual assessment in case of violation of the obligation to present documents, should be recognised as effective and dissuasive. Thus, as far as a violation of the obligation to present documents is concerned, the adverse consequences arising for the taxpayer from the restriction of fundamental rights imposed by the contested provision do not outweigh the benefit gained from the said restriction by society as a whole. [22.2.1, 22.2.2]

The Constitutional Court concluded that, in respect of a violation of the obligation to present documents, the restriction of fundamental rights imposed by the contested provision complies with the principle of proportionality. Consequently, the contested provision, insofar as it provides for a fine of 100 percent of the amount of tax payable to the state budget, applied without an individual assessment, for a violation of the obligation to present documents, is compatible with the first three sentences of Article 105 of the Constitution. [22.2.2]

On the moment when the contested provision becomes void

The Constitutional Court held that, in respect of the Applicant and the individuals to whom the contested provision is to be applied in administrative proceedings in court or in an institution as a result of a violation of the obligation to present documents, the contested provision is void as of the moment when the infringement of their fundamental rights occurred. In respect of other taxpayers, the contested provision is void as of the date when this judgment is published. In the above situations, the amount of the fine is to be individualised depending on the circumstances in which the respective violation was committed, for which purpose the first three sentences of Article 105 of the Constitution, the principle of proportionality, and the findings contained in this judgment are to be applied directly. [23]

The Constitutional Court ruled:

1. To recognise Section 34(1) of the law “On Taxes and Duties”, insofar as it, without an individual assessment, imposes a fine in the amount of 100 percent of the tax payable to the budget for engaging in economic activity after registering as a performer of economic activity but without registering as a payer of a particular tax, as being incompatible with the first three sentences of Article 105 of the Constitution of the Republic of Latvia.

2. In respect of Jānis Pīlāts and those taxpayers who have initiated and continue the process of protecting their fundamental rights using general legal remedies, to recognise Section 34(1) of the law “On Taxes and Duties”, insofar as it, without an individual assessment, imposes a fine in the amount of 100 percent of the tax payable to the budget for engaging in economic activity after registering as a performer of economic activity but without registering as a payer of a particular tax, as being incompatible with the first three sentences of Article 105

of the Constitution of the Republic of Latvia and void as from the moment when the infringement of their fundamental rights occurred.

3. To recognise Section 34(1) of the law “On Taxes and Duties”, insofar as it, without an individual assessment, imposes a fine in the amount of 100 percent of the tax payable to the budget for a failure to submit, within 30 days after the deadline set by the tax authority, tax declarations specified in tax laws, as well as the business and accounting records requested by the tax authority, without which the tax administration officers (employees) are unable to determine the amount of tax liability, as being compatible with the first three sentences of Article 105 of the Constitution of the Republic of Latvia.

The judgment of the Constitutional Court is final and not subject to appeal; the judgment enters into force on the day it is published.

The text of the judgment is available on the website of the Constitutional Court: https://www.satv.tiesa.gov.lv/wp-content/uploads/2020/06/2020-31-01_Spriedums.pdf

This release has been prepared to inform the public about the work done by the Constitutional Court. More detailed information on current issues, cases initiated and decided by the Constitutional Court is available on the [website of the Constitutional Court](#). You are also invited to follow the information on the Court's *Twitter* account [@Satv_tiesa](#) and *YouTube* [channel](#).

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