

Communication concerning the decision of the Curia of Hungary
in administrative case n° Kfv.I.35.594/2016

In the present case, the Curia had to address a number of legal issues, in particular as to the use of evidence obtained by way of secret information gathering and the possibility of reviewing the lawfulness of such evidence taking by an administrative court with special regard to the judgement of the European Court of Justice in case C-419/14.

The disputed contractual relationship made it possible for the tax authority to examine whether the taxable persons exercised their rights in an abusive manner and the relationship's intended purpose was tax evasion. Based on section 2, subsection (1) of the Taxation Act, the defendant authority was entitled to assess i. the real economic content of the parties' contract, ii. which party truly exploited the know-how transferred by the contract and iii. whether the sole purpose of the contract's relevant provisions – which provided for the relocation of the place of supply of services – was to create a more favourable fiscal environment. The Curia has already delivered some leading decisions regarding the abusive exercise of rights in tax matters (see cases n° Kfv.I.35.720/2015 and n° Kfv.VI.35.575/2012).

The Curia pointed out that, in the interpretation of the relevant national legislation, account should be taken of the case-law of the European Court of Justice – in particular, case C-255/02 (Halifax) and case C-425/06 (Part-Service) – in respect of tax evasion and the abusive exercise of rights, therefore a two-fold examination should be carried out: a) the real results from the operations concerned should be assessed and b) it should be apparent from a number of objective factors that the essential aim of the transactions concerned is to obtain a tax advantage. The prohibition of abusive practices is irrelevant in cases where the business operation may be carried out for economic reasons other than the accrual of a tax advantage. The Curia also established that it is of no significance whether the transaction formally complies with the relevant directive and the implementing national legislation. It is the responsibility of the national court to determine the real substance and significance of the transactions concerned, in so doing, it may take account of the purely artificial nature of those transactions and the links of a legal, economic and/or personal nature between the operators involved in the scheme for reduction of the tax burden. In paragraphs 35 and 42 of its preliminary ruling in case C-419/14, the European Court of Justice addressed the above issue and referred to the Court's well-established and unambiguous case-law.

The tax authority had the task of determining whether the parties' purely artificial transaction had served the sole purpose of obtaining an improper tax advantage. Tax administration is governed by the principle of freedom of evidence, which means that the parties are given the right to establish all the relevant facts of the case with any form of evidence and that the authority is entitled to freely assess the pieces of evidence submitted in order to establish the case's factual background. On the other hand, the principle of freedom of evidence does not entail that evidence taken in other proceedings may be freely used without any legal limitation and legality control.

In the present case, the pieces of evidence on the basis of which the tax authority established the facts of the case were obtained partly by way of secret information gathering and partly by way of ordering coercive measures in the investigation proceeding. With regard to the above, the question of whether the tax authority may use such pieces of evidence should be decided by taking into account these two different methods of evidence taking and the regulations governing them.

The judgement of the European Court of Justice in case C-419/14 showed that significant importance should be attached to the legality review of the secret gathering of information, the designation of the court to conduct such reviews, the determination of the procedural regime to be followed and whether administrative courts are empowered to review the legality of such evidence taking. Under the relevant legal provisions, the legality review of the secret gathering of information is to be carried out by criminal courts, hence, administrative courts are not empowered to do so. By virtue of section 76, subsection (2), point g) of the Act on the National Tax and Customs Administration and section 71/B, subsection (1) of the Code of Criminal Procedure, the legality review of such evidence taking by a criminal court within an adversarial procedure is a necessary precondition for the use of the pieces of evidence taken in such manner. The Taxation Act, the Code of Administrative Proceedings and the Code of Civil Procedure do not empower the administrative courts to conduct, in that regard, a test of legality and a test of necessity and proportionality, prescribed by the European Court of Justice.

The Curia did not agree with the defendant's argument according to which the above tests had been duly carried out by the investigative judge in a "disclosure process", since such disclosure had allowed for the use of the disclosed pieces of evidence only in the criminal proceedings. In addition, as the plaintiff correctly pointed out, the investigative judge's proceedings did not comply with the adversary principle, therefore such disclosure could not meet the requirements laid down in the judgement of the European Court of Justice.

The assessment of evidence obtained by way of secret information gathering and not subject to judicial authorisation is different from what was described above. In the case of these pieces of evidence, the conditions for the conduct of an adversarial procedure as set forth by the European Court of Justice were met, however, the party subjected to a search did not make use of that opportunity.

In summary, the Curia was of the opinion that records of telephone tapping produced in a secret gathering of information could not be used by the tax authorities and the administrative courts due to the lack of legal guarantees in their proceedings, while the latter may use the correspondence gathered by the investigative authorities in their criminal proceedings as pieces of evidence, because – due to the legal remedy scheme of the Code of Criminal Procedure – their use does not violate the parties' rights guaranteed under European Union law.

Budapest, the 17th of October 2017

Administrative and Labour Department of the Curia of Hungary