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PRINCIPLES AND EU TAXATION

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Introduction

Many factors in the last decades have contributed to a steep rise in the complexities of the circumstances of the reality. The unstoppable process of globalization, that is taking place in almost every field, is undoubtedly the main reason for this situation, that has led the national juridical systems to be progressively more intertwined, and the economic and legal events to be more multifaceted and detailed.

With this portrayal of the reality, some queries spontaneously arise. For instance, is it possible for the law to provide for an answer to all the possible different cases anymore? Is it the positive law still the most appropriate tool to face the issues arising from this context? What is the specific situation of the European Union and of the tax field in particular?

The following dissertation addresses these relevant questions and tries to answer them through the observation and description of the facts of the reality, through the opinion of the most eminent authors, and by referring to the most relevant legal sources in the matter, where present.

The thesis is divided in two main parts. The first one (Chapter I) deals with the concept of the principles of a legal order, analysing their deep essence and their relation with the moral values. In particular, it purports the idea according to which the principles play an essential role in the integration of the laws, and are crucial for their correct interpretation and application. Indeed, only a principle based approach to the law can make the legal rules adequate to regulate the constantly new circumstances presented by the hard cases to which they are called to give an answer.

After that, is demonstrated that new global challenges have brought to a widespread use of principles, and progressively to the development of a system of governance built up on transnational common principles, and based not on authority, on orders, but rather on consensual coordination, aimed to obtain the desired behaviours and flexible results.

The second part (Chapter II) of the thesis focuses specifically on the European Union case, in which is observed the same development of a governance and of the use of soft law. A governance that is multilateral, hybrid and based on coordination, in which the instruments of soft law are widely used to overcome the formalities of the EU hard law and the complex procedures for its adoption and emendation. With particular reference to the tax matter, it is then shown in detail as the development of the so called good tax governance have given the possibility to tackle efficiently the threats of the international tax avoidance, exactly thanks to the resort to a system of principles organized in the way described in Chapter I.

Chapter I

The first part of this work would inevitably deal with matters of legal theory and legal philosophy. Hereinafter, explanations and proofs of how this subject has concrete and practical implications will be given.

1. Principles

When it comes to talk about principles, the first point that needs to be clarified is the arguability and the permanent modification of the topic. What is now considered a principle might not have been so years ago; what someone defines as a superior common principle might be considered as a middle level principle by others, or just be given a different nomenclature; and discussions may well concern the feature of the principles themselves.

The analysis that follows will demonstrate as both the national and the international juridical systems are based upon “*current fundaments of principles and principals*”¹. In them, a law that expresses itself through factual circumstances and subsumption procedures, coexists with a law that resorts both to the pondering, without factual circumstances, and to the implicit and inexpressible meanings of the juridical order itself.

¹ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, El Fisco, Barcelona, 2017, p. 65

These meanings reflect themselves in principles of various levels and nature, that are prior to the positive law; and the jurist has the duty of searching for them, because they lead him to a real justice, perceived as such by the whole national and international community².

1.1 What are the principles?

Behind the hard substance of the juridical laws, hidden by the incessant stream of legislation, there are principles. Principles that precede, overcome and go beyond the law. The common principles are juridical criteria that cannot be extrapolated from the positive law. Simply because they do not derive from it. In fact, they are manifestation of a genetic and indefinite virtuality and expression of a pure spirituality that prevent them from simply ending up in a single and specific formulation. They are the embryonic cell, the germinal idea, the expression of the social consciousness, from which the *ratio iuris* of the law will develop. Their primary function is the “*interpretation and the orientation of the legislative policy and, in general, the development of the law, by giving it coherence and attachment to the social and spiritual conscience historically present in the community*”³.

Being the principles the common basis of the law and the directives for its interpretation, they represent an essential mean of integration of the positive law, showing at the same time a transcendental superiority that raises the moral values above the mere validity or applicability of the single provisions⁴.

Ronald Dworkin defines a principle as a “*standard that is to be observed, not because it will advance or secure an economic, political, or social situation deemed desirable, but*

² *Ivi*, pp. 65-66.

³ Betti E., *Teoria generale della interpretazione (Vol. 2)*, Milano, Giuffrè, 1955.

⁴ *Ibid.*

because it is a requirement of justice or fairness or some other dimension of morality”⁵.

The law, in fact, can't be reduced only to the positive law, since it exists from before the positivism: we find it in the values of the people and communities and in the common principles of coexistence⁶. When lawyers reason or dispute about legal rights or obligations, particularly in those hard cases when our problems with these concepts seem most acute, they make use of standards that do not function as rules, but operate differently: as principles indeed. All that is meant, when we say that a particular principle is a principle of our law, is that that principle is one which judges must take into account, if it is relevant in the specific case, as a consideration inclining in one direction or another.

The general common principles are intimately connected with the concept of natural law. Natural law which is made up of the basic rules that are pillars of the moral behaviour and expression of the fundamental shared values of a community. It creates a moral system, with a religious or laic fundament, that concerns both the moral autonomy of every subject, his deepest beliefs, basic certainties, intrinsic motivations; and his commitment towards the others and the society in which he lives in. Not even the absence of a specific religious inspiration can deny the absolute moral value of the natural law, because nobody can ignore basic moral principles like the individual dignity, the human rights and the responsibility for his own actions within the community.

The natural law itself is the source of that superior common principles that stay as basis of a legal system. The common principles derive and arise from the natural law, and they constitute a link between the moral aspect of the natural law and the human dignity and freedom. They are prior to every system, both economic, social and juridical and they establish unconditioned behavioural moral criteria that do not change across the time. They

⁵ Dworkin R., *Taking Rights Seriously*, Harvard University Press, Cambridge, Massachusetts, 1978, p. 22.

⁶ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 14.

are followed not because of the formal provision in which they are expressed, but because of the shared values of justice, equality, freedom and equity that they represent⁷. In fact, their origin lies not in a particular decision of some legislator or court, but in *a sense of appropriateness developed in the profession and the public over time*⁸. Their continued power depends upon this sense of appropriateness being sustained.

Legal principles are concretizations of legal values in the legal system, at a lower level of abstraction. Legal values and principles connect the legal system with the moral values and principles prevailing in society; the formers function as a kind of filter. Legal principles are vehicles in the movement back and forth between legal values and legal rules⁹.

According to Betti, there is a notable correspondence between the natural law deriving from the religious pact with God, that brings with itself the spiritual values of every religion to its observants, and the natural law originated from the social contract between individuals, based on ideals that born, grow and die together with the evolution or involution of the community. According to the ethical and moral vicissitudes of the moment, the common principle could be emanation of one or the other natural law. Thence, common principles can either be an expression of religious values or be closer to a laic solidarity; but they can also be a mean for the destruction of superior values through a shift in the primary social contract¹⁰.

Anyhow, whatever the source of the natural law is, his every matter, whether social, political or juridical, is at the same time a moral issue, and even when the principles are not

⁷ *Ibid.*

⁸ Dworkin R., *Taking Rights Seriously*, cit., p. 40.

⁹ Gribnau H., *Not argued from but prayed to. Who's afraid of legal principles?*, ejournal of Tax Research, Special Edition: Tribute to the Late Professor John Tiley, 12(1), 185-217.

¹⁰ Betti E., *Teoria generale della interpretazione (Vol. 2)*, cit..

visible at first, they are there and can sustain the natural law or negate it and maybe bring it to extinction¹¹.

People are members of a genuine political community only when they accept that their fates are governed by common principles, not just rules hammered out in political compromise. The members of a society of principles accept and recognise that their rights and duties are not exhausted by the particular decisions their political institutions have reached, but depend, more generally, on the scheme of principles those decisions presuppose and endorse. So each member accepts that others have rights and that he has duties flowing from that scheme, even though these have never been formally identified or declared. Nor does he suppose that these further rights and duties are conditional to his wholehearted approval of that scheme; these obligations arise from the historical fact that his community has adopted that scheme, which is then special to it¹².

An explicative argumentation regarding the pure essence of the juridical common principles, is given by Gustavo Zagrebelsky. He affirms that the principles are the vehicle, the means (*medium*) in which can be found on one side a theoretical openness to the value, and on the other side a practical openness to the rules; so an analysis on the nature of the principles reveals their function of both means through which the juridical world opens itself to the values, and means through which the values get into the juridical world.

This process takes place, according to the Italian constitutionalist, through the judgement of constitutionality of the laws, in which their compliance with the constitutional principles is evaluated. The principles represent the edge between the positive law and what is beyond it. In fact, despite being the constitutional principles contained in positive

¹¹ Rosembuj T., *I principi e la tax governance nell' Unione Europea.*, cit..

¹² Dworkin R., *Law's empire*, Hart publishing, Oxford, 2008.

provisions, they “*feed themselves through pre-positive conceptions*”¹³. That is the reason why the constitutional principles can be considered a bridge (*medium*) that joins the jurisprudence with the visions of the social life directly in force in the conception that the society has of itself.

Furthermore, Zagrebelsky believes that values, principles and rules can be thought as a sequence of inferences of an ethical-material validity, that reflects on the world of the formal juridical validity. For instance, the rule that punishes the crime of kidnapping implies, as its fundament, the principle of inviolability of the personal freedom, which in turn refers, as its justification, to freedom as a value; the rule that punishes the murder recalls, as its fundament, the principle of unavailability of the life from other human being, which in turn has its justification in the value of life; again, the rule on the fair taxation has as its fundament the principle of equality, that recalls the value of human dignity; and so on with umpteen possible examples.

Schematically, is possible to affirm that the world of the rules corresponds to the legislation; the world of the principles corresponds to the constitution; the world of the values corresponds to the culture¹⁴.

This scheme works as long as principles, values and rules are kept separated and do not get confused with each other. What distinguishes principles from values is not the object they concern, but the way it is concerned: a value, indeed, is something end in itself, is like a goal to be reached through teleologically oriented actions¹⁵. The evaluation of the legitimacy of the action is not contained in the value, whose only criterion is the instrumentality of the action to its realization, no matter which mean is used for it. As a

¹³ Zagrebelsky G., *La legge e la sua giustizia*, Il Mulino, Bologna, 2008 pp. 225-226.

¹⁴ *Ivi*, p.227.

¹⁵ Habermas J., *Factizitat und Geltung*, 1992. Translation to Italian: *Fatti e norme*, Guerini, Milano, 1996, pp. 302 e ss..

consequence, the noblest value could potentially justify the most despicable action. This is exactly the same query that also Nietzsche asked himself and to which he answered by saying that when the goals (values) are big, the humanity applies another criterion, and do not considers the crime as such any more, even in case of use of the most unbearable means¹⁶.

The principles, on the other hand, regard the means of our behaviour and not the goals. That is why, unlike the values, they contain certain normative aspects concerning our actions. Here, the criterion of evaluation of the legitimacy of the action is the deducibility from the principle.

In summary, the values are ahead of us, and they call us; the principles are behind us, and they push us. The formers indicate us the destination, but not the path; the latters the path, but not the destination.

On the contrary, the relationship between principles and laws is more debated (see *infra* 1.2), but the key is to clarify from the beginning the fact that a principle is something different from a very general rule, and at the same time is all the same a top value juridical rule because it operates as rule between rules and has a fundamental role in the juridical interpretation¹⁷.

The scheme portrayed by Zagrebelsky is clear and rather innovative. However it limits its considerations to that fundamental common principles expressed in the constitution. Actually, in addition to them, we find numerous other “kind” of principles emerging from the culture of the community. They are, as it will be explained in detail below (see *infra* 1.4), middle level principles, evaluative standards and transnational principles.

¹⁶ Nietzsche F., *Frammenti postumi 1887-1888*, in *Opere*, vol. VIII, t. 2, Adelphi, Milano 1971, p. 247.

¹⁷ Zagrebelsky G., *La legge e la sua giustizia*, cit., pp. 205-213.

As a matter of fact, in order for the principles to be able to exert some kind of practical effect, a process of concretization of them is needed. In fact, abstract principles cannot be applied directly unless they are specified and elaborated in concrete and often quite technical rules.

However, the possibility to arrive to a literal formulation of the principle is often discussed. Emilio Betti wrote that the principles, differently from the rules, are not susceptible of being transposed into a specific precept. In that case, they would be reduced to the same level of whichever law¹⁸. In his opinion, it is the jurisprudence the only source for the formulation of the principles, being it the responsible for the manifestation and the transfer of the social moral conscience into the juridical order.

But the consequent query that arises is: the jurisprudence creates or just declare the common principles? Carbonnier¹⁹ and Ganshof van der Meersch²⁰ agree on the fact that the principles are not a jurisprudential creation, but, as opposed, they exist from before the positive law and therefore judges have to research and apply them even when they are not formally contained in the letter of the law. *“The principles are created out of the jurisprudence, but once formed they impose to the judge and oblige him to make sure they are respected”*²¹.

Again, Modugno argues that the common principle cannot be enclosed in the letter of the law because its importance and its pondering value cannot get entrapped in a sentence: it

¹⁸ Betti E., *Interpretazione della legge e degli atti giuridici (Teoria generale e dogmatica)*, II ed., by G. Crifò, Giuffrè, Milano, 1971, p. 316.

¹⁹ Carbonnier J., *Droit Civil, Volume I et II (Prem. Ed.)*, in Presses universitaires de France P.U.F., Paris, 2004.

²⁰ Ganshof van der Meersch W., *Propos sur le texte de la loi et les principes généraux du droit*, in Journal Des Tribunaux, 1970.

²¹ *Ibid.*

arises from the underlying values that autonomously exist even before a literal interpretation, and it would exist even in the hypothesis of the lack of formulation²².

As far as I am concerned, together with a theoretical definition of the juridical common principles, the best way to get a plain and complete idea of them is to see their concrete application in hard cases. In order to do that, I will report the same two examples given by Dworkin in “Taking rights seriously”. In 1889 a New York court, in the famous case of *Riggs v. Palmer*²³, had to decide whether an heir named in the will of his grandfather could inherit under that will, even though he had murdered his grandfather to do so. The court began its reasoning with this admission: “*It is quite true that statutes regulating the making, proof and effect of wills, and the devolution of property, if literally construed, and if their force and effect can in no way and under no circumstances be controlled or modified, give this property to the murderer*”²⁴. But the court continued to note that “*all laws as well as all contracts may be controlled in their operation and effect by general, fundamental maxims of the common law. No one shall be permitted to profit by his own fraud, or to take advantage of his own wrong, or to found any claim upon his own iniquity, or to acquire property by his own crime*”²⁵. The murderer did not receive his inheritance. In 1960, a New Jersey court was faced, in *Henningsen v. Bloomfield Motors Inc.*²⁶, with the important question of whether (or how much) an automobile manufacturer may limit his liability in case the automobile is defective. Henningsen had bought a car, and signed a contract which said that the manufacturer’s liability for defects was limited to “making good” defective parts – “this warranty being expressly in lieu of all other warranties,

²² Modugno F., *Appunti per una teoria generale del diritto. La teoria del diritto oggettivo*, Giappichelli, Torino, 1989.

²³ 115 N.Y. 506, 22 N.E. 188 (1889).

²⁴ *Ivi*, at 509, 22 N.E. at 189.

²⁵ *Ivi*, at 511, 22 N.E. at 190.

²⁶ 32 N.J. 358, 161 A.2d 69 (1960).

obligations or liabilities”. Henningsen argued that, at least in the circumstances of his case, the manufacturer ought not to be protected by this limitation, and ought to be liable for the medical and other expenses of persons injured in a crash. He was not able to point to any statute, or to any established rule of law, that prevented the manufacturer from standing on the contract. The court nevertheless agreed with Henningsen. At various points in the court’s argument the following appeals to standards are made: (a) “*We must keep in mind the general principle that, in the absence of fraud, one who does not choose to read a contract before signing it cannot later relieve himself of its burdens*”²⁷. (b) “*In applying that principle, the basic tenet of freedom of competent parties to contract is a factor of importance*”²⁸. (c) “*Freedom of contract is not such an immutable doctrine as to admit of no qualification in the area in which we are concerned*”²⁹. (d) “*In a society such as ours, where the automobile is a common and necessary adjunct of daily life, and where its use is so fraught with danger to the driver, passengers and the public, the manufacturer is under a special obligation in connection with the construction, promotion and sale of his cars. Consequently, the courts must examine the purchase agreements closely to see if consumer and public interests are treated fairly*”³⁰. (e) “*Is there any principle which is more familiar or more firmly embedded in the history of Anglo-American law than the basic doctrine that the courts will not permit themselves to be used as instruments of inequity and injustice?*”³¹. (f) “*More specifically the courts generally refuse to lend themselves to the*

²⁷ *Ivi*, at 386, 161 A.2d at 84.

²⁸ *Ivi*.

²⁹ *Ivi*, at 388, 161 A.2d at 86.

³⁰ *Ivi*, at 387, 161 A.2d at 85.

³¹ *Ivi*, at 389, 161 A.2d at 86 (quoting Frankfurter, J., in *United States v. Bethlehem Steel*, 315 U.S. 289, 326 [1942]).

enforcement of a “bargain” in which one party has unjustly taken advantage of the economic necessities of other...”³².

1.2 Principles based regulation and rule of law

Between a common principle and a (positive) law there are extremely relevant differences, both conceptual and applicative, as it has already been briefly outlined above. Notwithstanding that they are inevitably connected to each other, common principles and laws are two different concepts, and many authors have tried to characterize and describe this distinction underlining various aspects. Actually, is exactly trying to delineate this dichotomy that is possible to get to the widest and most complete portrayal of the real essence of the juridical principles.

The origins of this distinction have to be attributed to the dualism between the law seen as “substance” and the law seen as “form” that characterises our juridical tradition. Using the words of Zagrebelsky, the law as substance exists when it is experienced, being it an interior habit; as opposed, the law as form exists when its obedience is imposed, being it an external habit. The law as substance is assumed by people who submits to it; whereas the law as form is disposed by people who establish it. And again, the law as substance leans on spread social forces; while the law as form leans on centralized political power³³.

A principle based approach would depict a law structured by a coherent set of principles (about justice, fairness, procedural due process ect.) that judges would be asked to enforce in the fresh cases that come before them, so that each person’s situation is fair and just

³² *Ibid.*

³³ Zagrebelsky G., *La legge e la sua giustizia*, cit., p. 15.

according to the same standards³⁴. Legal principles function as essential criteria of evaluation, in the sense that law-makers are bound by them. This is a conception according to which the law is conceived as based on a coherent set of principles, which express the moral dimension of law itself³⁵.

Dworkin, moving from his steadfast idea explicitly oriented towards a principle based approach to the law, distinguishes between a “rule book conception” of the law, and a “right conception” of it³⁶. In his 1978’s treatise “Taking Rights Seriously” moreover, he states that the common principles are not to be confused with juridical and positive laws for a simple and logical reason: while the juridical laws are valid only if applicable to the specific and concrete case, the principles are valid regardless of their applicability in the specific case.

The difference between legal principles and legal rules is a logical distinction. Both point to particular decisions about legal obligation in specific and particular circumstances, but they differ in the nature of the direction they give. Rules, states the American jurist, are applicable in an *all-or-nothing* fashion, that means that either they are totally respected or they are totally violated³⁷. Given specific facts foreseen by the provision, the consequences, also them foreseen by the provision, will come as an automatic output. This is the same model of functioning described by Hans Kelsen through the famous and clear formula: if *a*, so *b*; and once established what *a* is, there is no room for *c*.

On the contrary, principles are not subject to this *all-or-nothing* way of application, but operate differently. They do not indicate juridical consequences mechanically deriving by the realization of the given events. Even those which look most like rules, do not set out

³⁴ Dworkin R., *Law’s empire*, cit., p. 243.

³⁵ Gribnau H., *Not argued from but prayed to. Who’s afraid of legal principles?*, cit..

³⁶ Dworkin R., *A matter of principle*, Harvard University Press, Cambridge, Massachusetts, 1985, pp. 9-11.

³⁷ Dworkin R., *Taking Rights Seriously*, cit..

legal consequences that follow automatically when the conditions provided are met. Moreover, they can have exceptions; can conflict with one another; can, for example, apply only when the conduct is reasonable; and they can give a guidance about how to deal with the points not expressly covered by the law. Since they are axioms of the juridical order, they push toward a certain direction without indicating specific actions or decisions connected to single cases. Inasmuch as they exist, their application is mandatory and serves as an explanatory criterion, even if the final determination of the action or decision needed, remains duty of the law and of the person in charge of applying it.

Besides, while potential conflicts or overlapping of laws are not allowed and in case are solved through the application of a clear and predetermined rule (*lex posterior derogat priori, lex specialis derogat generali, ect.*), principles, as opposed, can be balanced, which means relativized to each other, so that they can operate together.

Principles have a dimension that in rules lacks: the dimension of weight, or of importance. When principles intersect, the person in charge of resolving the conflict has to consider the relative weight of each. This cannot be an exact measurement of course, and the evaluation made will often be discussed. In spite of that, wondering how important or how weighty a principle is, maybe in comparison with others, is an integral part of the concept of principle itself.

As said, rules do not have this dimension. They might well be considered more or less important in the specific case, but we cannot say that one rule is more important than another within the system rule, even because this would entail that in case of conflict, one would supersede the other by virtue of its supposed greater weight. The decision as to which is the valid law, and which must be abandoned or recast, must be made appealing to considerations that are beyond the conflicting rules themselves. A legal system might

choose to regulate such conflicts by resorting to rules like the abovementioned *lex posterior derogat priori*, *lex specialis derogat generali*, *ect.* in case of conflicting laws, or opting for the rule enacted by the higher authority, or for the one enacted later, or again for the more specific, or also prefer the one supported by principles of a greater importance.

The principles are the mean to overcome this *all-or-nothing* or *aut-aut* logic typical of the laws. It often occurs, in fact, that the legislator, after having established a specific, clear and rigid rule, feels the need to soften its rigidity or to make its edges more flexible in a way that goes beyond the dual logic (*aut-aut*) of the law itself. This is the cases and the ways in which principles come to play their fundamental auxiliary role³⁸.

Principles, as said, often interact and conflict with one another, so that each of them that is relevant to a particular legal problem provides a reason arguing in favour of a particular solution, but does not stipulate it. “*When forming such rules principles will clash: one will push in this direction, the other in that direction*”³⁹. The person in charge to decide the problem (the judge) is therefore required to assess all the competing and conflicting principles that bear upon it, and to balance them, rather than trying to identify only one of them to be considered as “valid”⁴⁰.

The rules could also be schematically defined as algorithms of conduct because, once established their applicability, they automatically give the answer; while the principles, lacking a precise formulation, are a non-algorithm and are more “*a weight in favour or against an act or omission*”⁴¹.

Similarly to Dworkin, the German jurist Gustav Radbruch believes that the core feature of the principles and the fact that gives them an undisputed hierarchical supremacy over the

³⁸ Zagrebelsky G., *La legge e la sua giustizia*, cit. pp. 213-222.

³⁹ P. Scholten, “General Part” (*Algemeen Deel*), <http://www.paulscholten.eu/downloads/>, 1931, no. 252.

⁴⁰ Dworkin R., *Taking Rights Seriously*, cit., p. 72.

⁴¹ Alexander L., *What are principles, and do they exist?*, in San Diego Legal Studies Paper, 2013.

positive law, is their ability to give prevalence to the realization of moral duties and, accordingly, to create a law system that is not absolute, objective and permanent, but that, on the contrary, reacts to changes in the spiritual, social and historical developments of the community: a juridical system based on spiritual manifestations (the principles) that contain indications regarding what is good and what is evil, what is right and what is wrong. Thence, he imagines the moral duties as the ultimate pillars of the juridical system. The common principles are, according to this author, expression of a superior value of justice, that leads to the juridical certainty and that thus must prevail over the other possible values. The supposed superior level of the principles, brings with itself that the juridical laws, in case of contrast with one or more of the principles, become invalid and need to be removed, disappplied or substituted.

This is the so called *Radbruch's formula*. It implies that provisions lacking justice or equality, *ergo* going against fundamental common principles, are not only invalid, but also they do not deserve the definition of "laws". Radbruch, moving from the fact that both in the natural and in the rational law the validity of the law is always subject to the respect of the principles, considers the supremacy of the common principles over the ordinary positive laws as an undisputed truth⁴².

The theory elaborated by this German author, wants the common principles to be the elements that create a kind of super-legal (or metapositive) law system, able to judge the positive laws, to consider them contrary to the law (the *ius*) and, in general, to identify the violations hiding behind the positive provisions⁴³.

Something in a way similar, is the idea proposed by Gustavo Zagrebelsky, who claims that through the principles and due to their nature that is open to what is collocated beyond

⁴² Radbruch G., *Relativismo y derecho*, Temis, Santa Fe de Bogotá, 1999.

⁴³ Bix B. H., *Robert Alexy, Radbruch's Formula, and the Nature of Legal Theory*. *Rechtsteorie*, 37, 2006, pp. 139-149.

their formulation (the values), the validity of the law results as being subordinated to the social normativity. Not the other way around. The social life is obviously subordinated to the legal, but as long as the latter does not conflict with the former⁴⁴.

Falzea⁴⁵, on the other hand, focuses more on the relationship that exists between principles and ordinary laws, when referred to their application in concrete situations. According to this author, in order to depict a complete picture of this topic, a conceptual step back is necessary. First of all, at the highest level of importance we find the general interest of the community for the solution of problems arising in the social life. Problems that of course require a juridical answer. This is what he calls the fundamental juridical interest, expression of the primary demand of every community for the maintenance of their lifestyle. It represents the original phenomenon and the leading category of the entire juridical science.

With respect to this fundamental juridical interest, the juridical rules, whether principles or ordinary laws, are concepts that are necessarily to be collocated in a subordinated position. Nevertheless, the high level of indeterminateness that characterize the fundamental interest, prevents it from being considered as a practical and applicable solution for factual happenings. A process of progressive determination is therefore required. A process that, in its middle phases, sees the crucial contribution of both principles and positive laws. Both of them have in themselves the feature of the vagueness as well, but, proportionally to the approach to the final determination, it lessens progressively.

Essentially, the fundamental juridical interest and the others general interests in which it ramifies, end up in a complex of general principles on which the entire juridical system is deontologically organized. And, since the high rate of indefiniteness makes the principles

⁴⁴ Zagrebelsky G., *La legge e la sua giustizia*, cit. pp. 227-228.

⁴⁵ Falzea A., *Relazione introduttiva*, in *Atti del Convegno Linceo "I principi generali del diritto"*, Rome, 1992.

stay on the ground of what Falzea calls the *have-to-be* of the wished situation, instead of the *have-to-do* of the realizing action, they need acts of determinative intervention. Among them, a leading role is played by the production of laws.

So basically, this Italian scholar describes the law as a rule for the facts, built on the ground of the prevision of an event and the simultaneous prescription of an (re)action subject to the realization of the event itself; and the principle as an indeterminate rule, a feature that excludes a necessary link to a concrete circumstance and prioritizes its functions of orientation and planning.

It appears now clear the role of the principles as a mean to keep the unity and the coherence of the whole juridical system, being them the instruments for the jurist to confront the specificity of the single situation with the global and fundamental interest, which is the only criterion for the identification of the most appropriate juridical rule to apply.

1.2.1 The complexity of the facts

The corpus of principles describes a kind of law system characterized by the incalculability. As opposed, the positive law claims to be calculable and applicable like a machine. However, the incalculability of the facts and the unpredictability and complexity of the events, feed the values and the principles that are outside, before and beyond the juridical texts.

That being so, alongside the law, the role of direction and orientation played by the principles becomes fundamental. In fact, the uncertainty of the reality obliges to make a choice: either the law is changed anytime it gets overridden, or we resort to the principles, the only tools able to ponder and balance facts and interests. Clearly, it would not be

reasonable to totally substitute the laws with rules, the principles, totally lacking factual circumstances. Nonetheless, it is essential to recognize the crucial role of complementarity played by the moral dimension of values and by the general common principles, as an additional way to regulate human behaviours when, as nearly always happens, certain facts are insufficiently regulated or completely unforeseen by the laws, but are anyhow faceable resorting to this criteria, that are outside the positive law⁴⁶. “*The principle is something external to the rules which helps one to construe the rules and, as a consequence, enables the rules to be less detailed*”⁴⁷.

According to Pinder⁴⁸, in order to provide a juridical answer to practical cases, the approximation method through the principles is as valid as the formal law (what he defines “black letter law”). Indeed, although this method ignores the details and stays on a high level of abstraction, it has a crucial importance because it keeps the flexibility, the effectiveness and the constancy of the provision safe from the obstacles of the formalities and of the hard cases. Duty of the principles is therefore to clarify the general discipline in order to reduce the complexities of the detailed provisions.

That’s why what is often referred to as the “rule of law”, meaning the idea generally brought on by the positivist thinkers according to which the law should not resort to sources out of the positive rules, has no reason to be followed any more, at least in its more radical sense. The rule of law is supposed to work in a very (too) simple way: the positive law sets some clear conditions and, through a process of subsumption, when they are met by the facts, the outcome, scilicet the juridical answer required, comes automatically. A principle based approach, as opposed, would not disregard the central role of the law, but

⁴⁶ Rosembuj T., *I principi e la tax governance nell’ Unione Europea.*, cit.

⁴⁷ Avery Jones J., *Tax Law: Rules or Principles?*, in *Fiscal Studies*, 17(3), 1996, pp. 63-89.

⁴⁸ Pinder G., *The coherent principles approach to tax law design*, Economic Round-up, 2005.

would resort to the principles as a mean to determine the *ratio legis* of the law, so the direction to be followed.

The rule of law is sufficient and clear enough only when dealing with simple, stable and predictable actions, that do not include huge economic interests; whereas, in case of articulated actions, that take place in various locations and that include relevant economic aspects, only the principles are the tools that guarantee a higher level of juridical certainty⁴⁹.

As a corroboration of these thesis, Radbruch maintains that the law cannot overlook the “*nature of the things (Natur der Sache)*”⁵⁰, indicating through this expression the life in common, the relations and the vital organizations we witness in the society, and the facts that constitute it. Indeed, the nature of the things represents the historic, cultural, social, economic and spiritual substance, and the plurality of the cultural and social coexistence to which the law is called out to give an organization and an orientation. There is no law without reality, and no reality without a law regulating and determining its limits.

All these different elements highlighted by the abovementioned authors are part of that concept of complexity of the things that brings with itself the necessity of resorting to the system of the principles.

Nowadays the global context, through the interdependence of concepts, the exchange and replacement of institutions and the spreading of new demands often non locally perceived, demonstrates the complexity of the system and how every unforeseen event potentially exposes the communities to systemic risks, crisis, chaos, or even catastrophes (for

⁴⁹ Braithwaite J., *Rules and Principles: A Theory of Legal Certainty*, in Australian Journal of Legal Philosophy, 27, 2002.

⁵⁰ Radbruch G., *La naturaleza de la cosa como forma jurídica del pensamiento*, Universidad Nacional de Córdoba, Córdoba, 1963.

example: the financial crisis of 2008, the climate change, the phenomenon of the stateless income caused by the spreading of the digital economy ect.)⁵¹.

With respect to this, it is interesting to notice how, paradoxically, since the common principles do not have an organizational and ordering function, but rather they direct towards some specific goals, and, what is more, they were not born following to a specific process alike the other typical legislative acts, they introduce unpredictability in the system and can be considered as part of the causes of the complexity. Howbeit, as above partially explained, the principles are at the same time also the effects of the complexity of the system, being them the answer to the inadequacy of the juridical formalism, not any more able to deal with a reality progressively more indefinite and that tends to exclude from the positive rule exactly that conducts that bring the highest damage to the principles of justice, equity and equality⁵². The usage of the common principles, indeed, allows to integrate the laws from the outside and, by doing this, to solve their lacks and their imperfections⁵³.

So the principles simultaneously play a double role: on one hand they contribute to the rising of complexity of the system; on the other hand they constitute the only possible answer to it.

However it is worth remembering that although the principles usually have this hermeneutical, directive and integrative function, they are liable of having an immediate and direct application in the hard cases, without the mediation of any interposing legislative act.

With this background, is progressively imposing a *governance* that, unlike the rule of law, is teleological and based upon the principles. It is made of rules of conduct that for their

⁵¹ Rosembuj T., *Principios Globales de Fiscalidad Internacional*, El Fisco, Barcelona, 2013.

⁵² Rosembuj T., *I principi e la tax governance nell' Unione Europea.*, cit.

⁵³ Avery Jones J., *Tax Law: Rules or Principles?*, cit..

flexibility and ability to adapt to the different cases, constitute what is often referred to as the *soft law* (see *infra* 2).

1.3 Critics: the juridical positivism

Positivist thinkers have different opinions on many of the previous matters.

In order to extrapolate and analyse the main features of these discrepancies, it might be useful to draw up a schematic portrait of the main concepts of the legal positivism by listing their key tenets.

First of all, the law of a community is considered just as a set of rules directly or indirectly used for determining which behaviour will be punished or coerced by the public powers. These rules can be distinguished by specific criteria, by tests dealing not with their content, but rather with their pedigree or with the manner in which they were adopted or developed. This tests of pedigree may be used to distinguish valid legal rules from spurious ones or from other kind of social rules (for instance the moral rules) that the community follows but does not enforce through the public powers.

Secondly, the set of this (valid) legal rules is exhaustive of “the law”. Which means that if a certain hypothesis is not clearly covered by such a rule, then that case cannot be decided by applying “the law”. It will be decided by some official, maybe a judge itself, exercising its discretion, which implies reaching beyond the law for some other sort of standard to guide him in manufacturing a fresh legal rule or supplementing an existing one.

And finally, to say that someone has a legal right, or has some sort of legal power or a legal privilege or immunity, is equivalent to assert that others have actual or hypothetical legal obligations to act or not to act in certain ways touching him. Again, to say that

someone has a legal obligation is to say that his case falls under a valid legal rule that requires him to do or to forbear from doing something. In the hypothesis of the lack of such a valid legal rule, there is no legal obligation; it follows that when the judge decides an issue by exercising his discretion, he is not really enforcing a legal right⁵⁴.

What stands out from this brief description, is that legal positivism rejects the idea that legal rights can pre-exist any form of legislation; it rejects the idea, that is, that individuals or groups can have rights in adjudications other than the rights expressly provided in the collection of explicit rules, that compose the whole of a community's law. Individuals have rights only insofar as these have been created by explicit political decision or social practice.

Following to this conception of the legal world, the attribute of *legality* (the conformity with the laws, meaning *leges*) is absolutely dominating over the attribute of *legitimacy* (the conformity to "the law", meaning *ius*). Solely the legality of a rule, coming from the fact that it has been adopted following to a specific procedure, gives it the legitimacy. It looks like the law (*lex*) has totally absorbed "the law" (*ius*). A legal system can be judged as legitimate just by virtue of the legality of its rules. The legality is taken as the exclusive form of legitimacy⁵⁵. This conception is often referred to as *juridical nihilism*, to indicate the rigid separation of the form from the substance, and the identification of the law (*ius*) with the laws (*leges*), mere data of juridical technique⁵⁶. Paolo Grossi describe this situation with the following words: "*the law is now shrunk into the laws: a system of authoritative rules, of commands thought and wanted to be abstract and inflexible, unquestionable in their content, since not from its quality but from the quality of the*

⁵⁴ Dworkin R., *Taking Rights Seriously*, cit..

⁵⁵ Weber M., *Wirtschaft und Gesellschaft*, Tübingen, 1922.

⁵⁶ Zagrebelsky G., *La legge e la sua giustizia*, cit., pp. 88-90.

legislator they drag their authority”⁵⁷. According to Natalino Irti⁵⁸, the juridical nihilism is plainly expressed by the usage of the word “production” to indicate the process of creation of a law. Through this word, usually used for trading goods, results clear how is the mere will of the political power to choose if and how to create, produce indeed, a law.

From the positivist perspective, resorting to standards like the common principles, would introduce in the law a moral dimension, and this would inevitably lead to confusion and overlapping of law and moral, where keeping them strictly separated is one of the pillars of the legal positivism itself. A legal rule is such, thanks to its production in conformity with another rule, the so called “rule of recognition”⁵⁹, or “fundamental rule”⁶⁰, establishing the criteria of validity in that specific legal order.

That is why, for example, Irti criticizes Dworkin’s viewpoint by maintaining that the law (*ius*) exists only in the letters of the laws, and out of them we only have “*arbitrary and obscure will*”⁶¹. Being the principles independent from the legislative texts, therefore not explicit nor implicit in them, they are defined as mysterious entities, not different from transcendental values or natural rights. They would limit the judge in his decision, and, since they are not linked to any normative source, they would also end up in being at the mercy of who asserts to have discovered and reconstructed them. A form of pure voluntarism, or subjectivism.

In addition to that, in the opinion of Irti, the moral dimension proposed by Dworkin makes the jurist fall also into a form of sociologism, preferring the turbid and controversial positivity of the social facts to the positivity of the laws.

⁵⁷ Grossi P., *Mitologie giuridiche della modernità*, Giuffrè, Milano, 2001, p. 34.

⁵⁸ Irti N., *Nichilismo e metodo giuridico*, in *Rivista trimestrale di diritto e procedura civile*, LVI, 2002, p. 1161 ss..

⁵⁹ Hart H.L.A., *The Concept of Law*, 1961, Oxford University Press, Oxford, pp. 118 ss..

⁶⁰ Kelsen H., *Reine Rechtslehre*, Wien, 1960, pp. 217 ss..

⁶¹ Irti N., *Un diritto incalcolabile*, Giappichelli, Torino, 2016, p. 66.

Actually, Dworkin does not imagine the laws as transcendental rules, but simply identifies the existence of a moral dimension that is essential to complete and integrate the law, or even to change or ignore it. Common principles cannot be considered causes of the legal uncertainty; as opposed, their vagueness fosters a civil and productive discussion. Accordingly, Shrifin⁶² eloquently defines them as the first civic interpretative draft of the law.

What's more, paradoxically, the legal positivism, with its legalistic conception of the law, has to admit the existence of a space free from laws and therefore, since the law is only legislation, totally free from the law (*ius*). In this space, as a consequence, and here is the paradox, the jurist should be authorized to make absolutely discretionary choices.

It results clear as the pretension of the positivists to expunge from the law everything out of the positive laws, instead of assure its objectivity, certainty, pureness and transparency, paves the way to arbitrariness. Facing the reality that the juridical experience is not strict application of the laws, but inevitably implies judgements on elements on which the rules do not have control, the positivist thinker affirms that there is a space always remaining subject to the personal and subjective will of the jurist.

In reality, what should be done is resorting to the juridical common principles, expression of what stays around and beyond the law, where the conceptions and the roots of the social relations from which the law itself has its origins can be found. This approach, despite not being formally legislative, would not be malfeasance, deceit or expression of personal arbitrariness, but, on the contrary, a honest research of a common substance⁶³.

⁶² Shrifin S. V., *Inducing Moral Deliberation: On the Occasional Virtues of Fog*, Harvard Law Review, 123, 1214-1246.

⁶³ Zagrebelsky G., *La legge e la sua giustizia*, cit., pp. 231-235.

1.4 Different levels of principles

The principles can be classified in different typologies or different levels. As said in the beginning, the categorization of the principles is not always pacific and moreover is variable across the time. Someone may elaborate an articulated differentiation, and some other a less detailed one; whereas others may have a diametrically opposed approach.

1.4.1 Superior common principles

The superior common principles are the means through which the supreme values, containing the founding and common values such as the ones of justice, freedom and solidarity, are recognized.

Falzea⁶⁴ distinguishes these superior principles in: *common (or unexpressed) principles*; and *fundamental (or expressed) principles*. The formers are the directives inductively extrapolated by the ordinary laws of our entire legal system or of parts of it (for example specific institutes or subjects) that rationally sustain from the inside the systematic unity of the juridical system, and are not expressed by specific formulation, neither in nor out of the constitution; the latters are the targets and the values that the legislator has placed at the top of the juridical system, in order to make sure that the whole lifestyle of the society, in its vocation for an incessant improvement, can evolve and move towards them. This means that the fundamental common principles, that are expressed by the constitutional provisions, through their aspiration to be expression of the social wills and values, represent an explicit purpose of correction and of optimization of the social lifestyle in a specific historical period.

⁶⁴ Falzea A., *Relazione introduttiva*, cit..

1.4.2 Middle level principles

On an hypothetical hierarchical scale of principles, we find on the top level the superior common principles, first and direct manifestation of the values. After them, on the lower stage, there are the common principles of middle level.

The middle level principles approach the juridical rules from a position external to them, moving from criteria of evaluation that are in accordance with the superior principles and with the moral values.

Core feature of these principles is their being external to the juridical positive system, and therefore the fact that their influence is given by a system of orientation different from that of the laws.

The middle level principles express the need for a shared specification impossible to be found in the abstractness of the superior common principles. On the one hand they are still undetermined and abstracts as the superior common principles; but on the other hand they have some different qualities and particularities. They are more specific and binding compared to the superior principles, since they are closer to the concrete cases. Indeed, they put in contact the generality and the abstraction of the superior common principles with the exigencies of the specific legislation of certain juridical areas.

Basically, the goal of the middle level principles is to create a bridge, able to connect the concrete circumstances and the juridical rules, with the superior common principles and the moral values, this way facilitating the role of the jurist of highlighting the legal and moral characteristics of the hard cases, supporting the research and realization of justice and chasing objectives of coherence and integrity of the juridical system.

The middle level principles do not recall the ultimate fundament of the social life, but the moral autonomy of the individual that, together with the moral autonomy of other

individuals, creates an area of public consensus, even when contrasts and conflicts between moral autonomies show up. This, together with their accordance to the superior common principles, makes the middle level principles being an instrument to defend the general interest of the community, without hindering the pluralism of the moral autonomy⁶⁵.

Sunstein⁶⁶ defines the middle level principles as “incompletely theorized agreements”. The reason for this expression lies in this: that the middle level principles are undetermined like the superior principles, but, differently for them, they represent intermediate shared values that cannot benefit from a sufficient consensus to be defined as common. Anyway, they are shared enough to be able to make certain evaluative widens or restrictions of ordinary laws.

The acceptance of a superior common principle, in fact, does not automatically implies its acceptance also in concrete cases, or, vice versa, the acceptance of a middle level principle does not necessarily brings with itself an accordance on the superior principle. The utility of the middle level principles is exactly of avoiding that, in specific cases, the superior common principle could lose its general consensus. This duty is easily fulfilled by the middle level principles since, at least in their essential points, they are in accordance with the superior ones.

1.4.3 Evaluative standards

Evaluative standards are precepts of an extra-judicial nature, that turns into juridical because of their inclusion in the rule⁶⁷. They are middle level principles that are inserted in the juridical rule.

⁶⁵ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit..

⁶⁶ Sunstein C. R., *Incompletely Theorized Agreements Commentary*, Harvard Law Review, 108, 1733-1772.

⁶⁷ Falzea A., *Ricerche di teoria generale del diritto e di dogmatica giuridica*, Giuffrè, Milano, 1999.

Evaluative standards are expression of a flexible law whose purpose is, through their indefiniteness, to widen the juridical effects of the rigid laws.

General clauses that are often found inside the laws like “honest living”, or “according to best (accounting, banking ect.) practices” and so on, are exactly evaluative standards.

The widening function of the evaluative standards takes place inside the law. That being so, when an evaluative standard is used, we are not resorting to extra juridical concepts but to pure juridical ones. The juridical rule replace the virtuality of the common principle and turns the extra juridical concepts into juridical ones. That is why evaluative standards cannot be confused with middle level principles: the formers are attracted by the juridical rule and inserted in it; the latters are out of the juridical rule and attracted by the superior common principles.

Regarding the source from which the evaluative standards come from, it has to be noticed as, especially in the last decades, the ones concerning the economic, financial, insurance and fiscal policy are, for the majority, coming from the deliberations of international organizations, both public and private, rather than from the national concepts of the community.

1.4.4 Transnational principles

Moving from the verification of the existence of a huge transnational legal system, meaning through this expression a complex of rules including whatever kind of law aimed to regulate cross-bordering events or behaviours regarding States and multinational enterprises as well as individuals and minor companies, we observe how the internationalization and the globalization of the relations between States and private agents, stimulates a dynamic process of monism in the convergence around transnational

principles and values generally recognized (“complying adjustment”), together with the traditional process of dualism in the conventional interrelation between national and international rules (“adapting adjustment”). In this way, the incorporation of general international rules, makes the national juridical order open itself to transnational rules and adopt them, through the “complying adjustment”, as if they were domestic rules: the transnational common principles⁶⁸.

The transnational principles are the orientations and values that are set and formulated in the agreements reached within the wider communities in which the national ones take part. They enter the domestic legal system as a complying adjustment to the values and principles coming from non-treaty international sources, and are implemented as if they were born domestic.

2. From hard to soft law – A global governance

The term “governance” is a multi-faceted concept which is fluid and variable in content. In one sentence it could be defined as “*horizontal networks and authority relationships defined by flexibility and voluntary rules*”⁶⁹. The usage of the word governance reflects a shift of attention from the formal legal order strongly related to the sovereign state, to informal relationships in which responsible citizens and organisations are engaged⁷⁰.

⁶⁸ *Ibid.*

⁶⁹ Mörth U., “Introduction”, in U. Mörth, *Soft Law in Governance and Regulation: An Interdisciplinary Analysis*, Edward Elgar Publishing, Cheltenham, 2004.

⁷⁰ Gribnau H., *Soft Law and Taxation: EU and International Aspects*, *Legisprudence* Vol. II No. 2, 2008, pp. 19-20.

The governance, so the govern without authority, is a process made of agreements and of non-rigid recommendations, that stands upon benchmarks, peer reviews, best practices and principles, in order to create shared expectations of compliance⁷¹. Governance structures promote proceduralisation, engagement, and dialogue in order to enable agreement, compromise, and consensus.

The concept of governance could also be described as a system with an intrinsic international inclination and a content that is based not on authority, on orders, but rather on consensual coordination, aimed to obtain the desired behaviours and flexible results. This results are pursued through the usage of instruments of principles and evaluation criteria of international institutions that promote and direct the conducts of the participants⁷².

“Global governance is governing, without authority, relationships that transcend national frontiers” said in 1995 Finkelstein⁷³. This definition is correctly wide. Governance indeed accommodates both governmental and sovereignty free actors; both ad hoc and institutionalized; as well as both formal and informal processes.

Key concepts, in defining what governance is, are: participation, responsibility, interaction, coordination, consensus, transparency, effectivity and efficiency, predisposition for an institutional and processual answer, soft law. All of these are elements that describe the way transnational actors interrelate with each other in the global governance.

What prevails in the governance are the goals, the targets to be reached through informal, flexible and soft juridical sources, evidently different from the rigid sources typical of the hard law. Indeed, as said before, the governance approach shifts the focus to the processes

⁷¹ Kamto M., *Droit international*, Pedone, Paris, 2013.

⁷² Dingwerth K. & Pattberg P., *Global Governance as a Perspective on World Politics*, in *Global Governance*, 12(2), 185-203.

⁷³ Finkelstein L. S., *What is Global Governance?*, in *Global Governance*, 1(3), 367-372.

and actors that are part of policy-making or offer alternative sources of governing, stressing the importance of different stages of policy-making and modes of governing. These processes and actors are ignored by the “*traditional focus on the core institutions of government, namely parliament, executive, administration and party politics*”⁷⁴. In a way, traditional formal and hierarchical governance is complemented by modes of informal governance⁷⁵.

For instance, the activity of the G20 is a clear example of the usage of governance instruments. The G20, which is a political organization of an informal kind, establishes directives for States and private agents through the technical support of other international bodies and group works, and is founded on the international economic cooperation, with the aim of safeguarding the global stability and the management of systemic risks. In fact, the G20 does not exert an authority on the States, both its members or not. As opposed, its decisions are expressed through recommendations that the States are interested to respect.

Thus, moving from the idea of a global governance, one can see how a system of transnational common principles, that are a multilateral expression of consensus or obedience, is progressively organizing. Having as a result a cultural integration of the values and principles coming from the different juridical systems⁷⁶.

It is just the case to briefly note how this new system of regulation might bring some risks with itself. As Bovens maintained, there is a risk of fragmentation of policy and political decision-making, which may be at odds with the need for continuity. This fragmentation also makes it more difficult to check who exactly can be held accountable for deciding

⁷⁴ Smismans S., *Law, Legitimacy, and European Governance*, Oxford University Press, Oxford, 2004, pp. 25-26.

⁷⁵ Gribnau H., *Soft Law and Taxation: EU and International Aspects*, cit., p. 22.

⁷⁶ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 56-63.

what. This kind of shared responsibility leads to “the problem of many hands”: if no one can be held accountable, then no one needs to behave responsibly⁷⁷.

2.1 Soft law

The juridical instrument through which the governance has progressively imposed all over the world and in several different juridical matters, as said, is a kind of regulation characterized by its flexibility and non-binding nature (not directly enforceable), able of exert its influence thanks to a process of voluntary compliance: the soft law.

However, technically speaking, the concept of soft law is a subject of great debate among legal scholars.

First of all, soft law is a conventional term coined by the doctrine whose first purpose is to mark a dividing line with the hard law. Soft law is what it is not: it is not hard law⁷⁸.

Abbott and Snidal⁷⁹ describe hard law as having three dimensions: the precision of the rule, its binding nature, and the delegation for its implementation and interpretation to a party third from the decision maker. They defined hard law as a clear-cut legally binding obligation, or an obligation that can be made more precise through court rulings or regulations, and whose interpretation and implementation is delegated to a different authority. For these authors, the realm of soft law begins once a rule is weakened along one or more of these dimensions.

⁷⁷ Bovens M., *The Quest for Responsibility: Accountability and Citizenship in Complex Organisations*, Cambridge University Press, 1998, pp. 45 ff.

⁷⁸ Shaffer G.C. & Pollack M.A., University of Minnesota Law School Legal Studies Research Paper Series, 2010, pp. 714-715.

⁷⁹ Abbott K.W. & Snidal D., *Hard and Soft Law in International Governance*, International Organization, Vol. 54, 2000, pp. 421-422.

Beside what it is commonly called hard law, there are many instruments which are not legally binding, and together are granted the term soft law. Soft law is therefore an expression that indicates norms or principles that, being them not legally binding, are followed on a voluntary basis. In spite of that, as it will be explained, they are anyway capable of exerting some relevant juridical effects.

Quoting Francis Sneyder, soft law is a union of “*rules of conduct which in principle have no legally binding force but which nevertheless may have practical effects*”⁸⁰. Other authors, with a more specific reference to the European Union, give a definition of soft law as “*rules of conduct which find themselves on the legally non-binding level (in the sense of enforceable and sanctionable), but which according to their drafters have to be awarded a legal scope, that has to be specified at every turn and therefore do not show a uniform value of intensity with regard to their legal scope, but do have in common that they are directed at (intention of the drafters) and have as effect (through the medium of Community legal order) that they influence the conduct of Member States, institutions, undertaking and individuals, however without containing Community rights and obligations*”⁸¹.

The term “soft law” is used in many contexts and for a wide array of instruments including without limitation: declarations, resolutions, recommendations, codes of conduct, guidelines, standards, charters, reports, opinions and any other act that, though having in themselves an expectation of having a certain kind of influence and effects on the behaviour of the addressees, are not pure legislative acts, and therefore are not able of exerting a binding power.

⁸⁰ Sneyder F., *Soft Law and Institutional Practice in the European Community*, in S.MARTIN, *The Construction of Europe: Essays in honour of Emile Noël*, Dordrecht, Kluwer Academic Publishers, 1994, p. 198.

⁸¹ Borchardt G. & Wellens K., *Soft Law in European Community law*, Springer Netherlands., 1989, p. 285.

Coordination, cooperation, and finalistic approximation to the targets and to the governance, are the key points regarding the system of soft law.

According to the traditional formal definition, a source of law (of hard law) is the act or fact expressly authorized by the system to produce juridical rules and to introduce modifications and innovations in the system itself⁸². Soft law, by contrast, is produced by subjects non authorized by any law on the production, and that do not follow any previous law on the procedure.

Besides, there is no constitutional nor legal provision in the domestic body of laws of any State which provide a specific status for soft law.

Scholars have not reached consensus on why States use soft law or even whether soft law is a coherent and analytic category. In part, this confusion reflects a deep diversity in both the types of international agreements and the strategic situations that contribute to produce it⁸³. Soft law instruments, in fact, are usually used as a substitute for hard law in legally or politically sensitive areas, in which it would be impossible or undesirable to adopt binding norms. Instead, parties prefer to specify softer and more malleable parameters in order to obtain the wanted behaviours and the desired results.

Since it is not binding, soft law will be followed as long as it creates a positive perception in its favour among its recipients. This positive perception is capable of making soft law acquire a standard and a strongly persuasive character. The OECD Model Convention and the OECD Commentaries⁸⁴, as well as the OECD Transfer Pricing Guidelines, are common examples and evidences of what has just been said.

The ratio that stays behind the adoption of these kinds or rules is that they allow States to solve straightforward coordination issues in which the existence of a focal point is enough

⁸² Bin R. & Pitruzzella G., *Diritto Pubblico*, Giappichelli Editore, Torino, 2002, p. 267.

⁸³ Guzman A.T. & Meyer T., *International soft law*, in *Journal of Legal Analysis*, 2(1), 2010, pp. 171-226.

⁸⁴ French Council of State Report, *Le droit souple*, EDCE, 2013, p. 27.

to generate compliance. In addition to that, usually soft rules are acts that require a short amount of time for the adoption as well as a quick procedure of their emendation, especially in technical matters in which constant revisions are necessary. In fact, regarding the last point, states choose soft law when they are uncertain about whether the rules they adopt today will be desirable tomorrow, and when it is advantageous to allow a particular State or group of States to adjust expectations in the event of changed circumstances. Moving from hard to soft law makes it easier for such States to renounce existing rules or interpretations of rules and drive the evolution of soft law rules in a way that may be more efficient than formal renegotiation⁸⁵.

What's more, the lack of pure legal effects of the soft regulation makes possible on the one hand to apply pressure on States that are not complying with it without provoking their open opposition, and, on the other hand, to avoid forcing them to ratify it as a real treaty would require⁸⁶.

When we talk about soft law we refer to a complex of instruments, through which rules of conduct are established, that, despite lacking a legal binding effect, are able to influence and orient the behaviour of the addressees. In case of violation of provisions of soft law, indeed, some concrete consequences are produced. The soft law rules, in fact, produce a so called "soft obligation", that undoubtedly can bring to sanctions of an economic, political or sometimes even administrative nature. These consequences, even though are not stated by jurisdictional authorities, are able to affect and influence actions and behaviours of the addressees of the soft law instruments. A non-compliant State can face repercussions such as a worsening of international relations, reduced leverage in negotiations, and/or a loss of

⁸⁵ Guzman A.T. & Meyer T., *International soft law*, cit..

⁸⁶ Focarelli C., *Diritto Internazionale*, CEDAM, Padova, 2012, pp. 255-258.

prestige⁸⁷. States can be forced to comply with certain soft law by a “international peer pressure” applied by the international community, for example by threatening to introduce economic sanctions if the rules are not followed. An example of this phenomenon may well be seen in Austria whose hesitation in the face of OECD Standard for Transparency and Exchange of Information crumbled quickly due to international pressure⁸⁸.

Regarding the kind of obligation deriving from the soft law, another point is worth a mention. Quite often, the consequences for not complying with soft law instruments are rather relevant. Sometimes so relevant that the addressees are *de facto* obliged to comply. In these cases, thence, we have a regulation that formally is not binding, but that, because of the heavy drawbacks originating in case of its refusal, turns, substantially, into a binding one. Such situation, consequently, makes raise a huge issue of democracy, and of popular representation and sovereignty⁸⁹. In fact, as long as the adherence to a corpus of rules is really made on a voluntary basis, the problem does not subsist; thus, the absence of a specific and formal procedure for the adoption of the provision, its being out from the sources of law specifically provided by the constitution and the fact that the body in charge of creating this rules might be not only not elected but even private, is not an issue at all. But when the adherence substantially turns into compulsory, these problems come to attention with all their strength. I will not elaborate further on this argument since it is not the object of this work, but in a discourse about soft law it is a matter that undoubtedly requires a deep analysis.

As examples of soft law in Italy we can recall the accounting principles or the self-regulation codes. The formers are a corpus of rules created by the OIC, (Organismo

⁸⁷ Walter L., *Soft Law in der Praxis*, in Lang/Schuch/Staringer (eds.), 2005, p. 24.

⁸⁸ Jirousek H., *Die Reaktion Österreichs auf den Vorwurf der “Steuerhase”*, in Hummer (ed.) *Die Finanzkrise aus internationaler und österreichischer Sicht*, 2011, p. 175.

⁸⁹ Bin R., *Soft law, no law*, in Somma A., *Soft law e hard law nelle società postmoderne*, Giappichelli, Torino, 2009, pp. 33, 38.

Italiano di Contabilità) that is not a constitutional organ and does not have legislative power, but is a private foundation, legislatively regulated, that has created the accounting principles rules for Italy. The latter are complex of rules adopted by private entities in order to give themselves criteria of regulations. For instance the Corporate Governance Code of Borsa Italiana is a self-regulation code, and its rules are adopted on a purely voluntary basis.

Examples of international soft law, instead, can be found in the international commercial law, for instance in the UNIDROIT Principles for International Commercial Contracts, or again in the international accounting principles IAS/IFRS. In addition to them, also the green books and the white books are examples of soft law. They are instruments frequently used by the EU Institutions, especially the Commission, to foster consultations and discussions on certain topics and issues (green books), or in order to express concrete proposals of legislation and bases for the political discussion (white books, that often follow the green ones).

In addition to them, others examples of soft law will be presented in more detail later on in this thesis.

1.2.1 The transnational legal process and the criteria of creation of expectations

The soft law, that creates and stimulates the governance, can be of two categories: we either have the transnational legal process that creates the middle level principles in the shape of evaluative standards; or we have the common principles, both superior and of middle level, that create shared expectations of realization.

The transnational legal process, as theorized by Hongju Koh, is the “*description in theory and practice of how public and private actors – nation-states, international organizations,*

*multinational enterprises, non-governmental organizations and private individuals – interact in a variety of public and private, domestic and international fora to make, interpret, enforce, and ultimately, internalize rules of transnational law*⁹⁰. This interaction between international actors, produces a number of international juridical acts that are interiorized by the States through a mechanism of obedience that, differently from compliance, lies upon the conviction of the fairness of that rules and so upon a voluntary subjection to them. Hence, the perception is of an obliged behaviour, even in the absence of a real duty of compliance⁹¹. The international evaluative standards, that have to be relevant, universal, flexible, widely accepted, and revisable, get an obedience that does not come from treaties or other forms of hard law, but comes from acts like informal agreements, best practices, codes of conduct, action plans or technical standards, issued by international bodies such as the International Monetary Fund, the World Bank, the OECD, FATF, etcetera. The transnational evaluative standards are usually interiorized through domestic provisions. That is what happened, for instance, with the BEPS Action Plan in which some provision were indicated as minimal standards, which means that is demanded their formalization and inclusion in the national law⁹². Basically, the minimal standards are the Actions of the BEPS (or referred to any other act) that everyone agrees to insert in the national legal system through a domestic provision.

Whereas, the creation of shared expectation is undoubtedly the key strength of the soft regulation. This concept relies on (soft) rules that are addressed to the community of the States and not to a State as a single agent and that, despite their non-binding nature, which is beyond any dispute, are able to create such expectations of compliance from every single

⁹⁰ Hangju Koh H., *Jefferson Memorial Lecture – Transnational Legal Process after September 11th*, Berkeley Journal of International Law, 22, 337-354.

⁹¹ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., pp. 59-60.

⁹² Falzea A., *Ricerche di teoria generale del diritto e di dogmatica giuridica*, cit..

State, that this makes the addressees apply the soft rules in order to comply with these expectations of the other agents; this way increasing, in a certain sense, the strength and the authority of the soft law itself⁹³.

3. Principles in tax law

All these matters obviously have their expression, among the other juridical areas, in the tax field.

With reference to the financial and fiscal law the role of principles is evident and essential. Benvenuto Griziotti⁹⁴ identifies three superior common principles that constitute the basis and the guide of the financial and fiscal system, and he demonstrates once again the importance of them as instruments of justice. They are the commutative principle, the solidarity principle and the principle of the extortions.

First of all, the commutative - or reciprocity - principle, indicates the necessary correspondence between the received or requested public services and a counterpayment, that would be commensurate with the ability to pay principle. It can be considered the pillar of the fiscal legitimacy. The levying of the tax is the natural outcome and the answer to the relation existing between the duty of the taxpayer to participate to the public expenses, and the correspondent duty of the State to organize and supply public services and goods. The commutativity confirms how the correspondence between the tax and the public service is essential to accomplice the tax duties, and also how the State does not

⁹³ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., pp. 61-62.

⁹⁴ Griziotti B., *Saggi sul rinnovamento dello studio della scienza delle finanze e del diritto finanziario*, Giuffrè, Milano, 1953.

have an imperative and coercive levying power, but how, on the contrary, its levying power is a redistributive tool based on the ability to pay principle. An individual obeys to the command of the tax law if the legislator is complying with its duties as well. Otherwise he shows reticence or directly resistance. The reciprocity principle goes together with the paradigm of justice⁹⁵. Therefore, it can be inferred that the tax payment derives firstly from an ethical rule and just in second place from a juridical rule, because the reciprocity value expressed by the ability to pay principle is moral and social, even before being constitutional.

Secondly, the principle of financial solidarity, that responds to social, economic and political demands through tax benefits aimed to satisfy public needs, has relevant similarities with the previous one. Indeed, also the solidarity is primarily an ethical value, that specifies as taxes have to fulfil a social function towards the most vulnerable subjects.

And finally, with the principle that Griziotti names of the extortions or of the parasitism, he indicates the expenses or the illicit tax revenue destined to enrich some specific social groups or also the levying of taxes without respecting the ability to pay principle. A kind of financial illusion or institutional corruption, it might be said. Through this third principle the author underlines how from the human behaviours derive not only the principles and the values that lead to justice, but also the individual interests that affect the correct functioning of the institutions of the public finance and harm the general interest⁹⁶.

From this portrait made by Griziotti, it can be deduced that the reality of the facts is more relevant of both the law and the will of the tax payer, consequently showing another superior common principle: the principle of the economic reality, in contrast with the juridical formalism.

⁹⁵ Rosembuj T., *Tax morale*, El Fisco, Barcelona, 2016.

⁹⁶ *Ibid.*

This other principle brings with itself that the fiscal justice cannot take into consideration only the certainty of formal law; in fact the provisions contrasting with the rights and the freedoms of the tax payer must not be applied. In addition to that, to get to a true fiscal justice it is essential to consider the real facts and their economic function. For instance, without this approach, it would be impossible to tackle the aggressive tax planning, the abuse of right and the tax arbitrage as results of unfair laws⁹⁷.

Thence, the juridical formalism is not often the good way to get to fair decisions and it can be maintained that the concept of financial justice basically means to make the principle of the economic reality and the law be in agreement, and to facilitate an adaptive interpretation (*interpretation abrogans*) in order to provide for the insufficiencies of the law itself⁹⁸.

Principles reveal their importance in the tax field in other ways as well.

They have a primary role in the fight against the tax avoidance and the creative compliance. Through these two practices, the legal certainty is completely eliminated and the rule is reduced to an instrument in the hands of the taxpayer, or more precisely, in the hands of unscrupulous tax professionals.

Indeed, the creative compliance involves “*finding ways to accomplish compliance with the letter of the law while totally undermining the policy behind the words*”⁹⁹. It consists in the research of omissions or of gaps between the letter of the law and its goals, to be exploited in order to get to a “*perfectly legal non-compliance*”¹⁰⁰, which means a formal compliance but a substantial non-compliance.

⁹⁷ Rosembuj T., *Minimizaci3n del impuesto y responsabilidad social corporativa*, El Fisco, Barcelona, 2009.

⁹⁸ Rosembuj T., *I principi e la tax governance nell’ Unione Europea*, cit., p. 39.

⁹⁹ McBarnet D., *When Compliance is not the Solution but the Problem: From Changes in Law to Changes in Attitude*, Working Paper n. 18, ANU Research Publications, 2001.

¹⁰⁰ *Ibid.*

Two are the main factors that contribute to the practice of creative compliance. One is the nature of the law itself and the process for its creation. *“The law-making process leads to lobbying and compromise, and legislators cannot address every contingency that might arise. So drafting is inevitably fallible”*¹⁰¹. The other and more fundamental factor, is that *“it is in the nature of the law that it is open to different interpretations, and that its meaning and application are arguable. Creative compliance, however, does not arise deterministically from the nature of the law. It also requires a particular attitude to the law, an attitude which, far from seeing the law as an authoritative and legitimate policy to be implemented, sees it as a “material to be worked on”, to be tailored, regardless of the policy behind it, to one’s own or one’s client’s interests. And it also requires active legal work”*¹⁰².

The law is open to alternative interpretations. Innovations in practice can leave the law behind. But grey areas, alternative interpretations and innovative legal forms do not just arise “naturally”. Rather, they may be motivated precisely by the desire to outflank the law. Indeed, creative compliance involves careful scrutiny of the law in order to seek out material for an actively constructed alternative and innovative arguments and legal forms¹⁰³.

Hence, what needs to be fostered is a change of attitude to the law, in which it is seen not as a game of words, a material to be worked on to one’s own or one’s client’s advantage, but as an instrument of legitimate policy to be respected, with the policy, not just the words, looked to as the measure of compliance.

¹⁰¹ McBarnet D., *Law and capital: The role of legal form and legal actors*, International Journal of the Sociology of Law, 12 (3), 1984.

¹⁰² *Ibid.*

¹⁰³ McBarnet D., *When Compliance is not the Solution but the Problem: From Changes in Law to Changes in Attitude*, cit..

More practically, since rigid detailed rules have been recognised as providing too fertile a soil for creative compliance, the only way to efficiently tackle this harmful practice is resorting to principles, focusing on the substance rather than on the form, and stressing principles like the general anti abuse clauses. Only by means of the joint usage of principles and rules it is possible to create a legal system able to prevent the manipulation of the details of the law, made through harmful business behaviours¹⁰⁴.

¹⁰⁴ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 52.

Chapter II

4. EU tax governance

In order to draw a complete portrait of the tax governance of the European Union, it is necessary to clarify which is exactly the real power of the European institutions in the tax matters and how their authority is exerted in such a delicate field in which the Member States have always shown reluctance in delegating their levying power to the European Union.

Traditionally and ideologically, the EU Member States believed that the delegation of their powers to the EU institutions could concern solely technical and largely apolitical issues of market regulation, whereas the control of politically salient matters implying redistributive and ideological conflicts, like the taxing power, should have been retained by the States. This attitude, together with the fact that taxation remains one of the few policy fields in the European Union still subject to the unanimity rule, have brought to the development of what Genschel and Jachtenfuchs define the “*no taxation thesis*”¹⁰⁵. This idea, that affirms the existence of a mild control of the EU over national taxation and the substantial tax autonomy of the Member States, has been undoubtedly overcome by the facts of the last years.

The EU’s regulatory power over taxation is strictly linked to its competence for developing the “Single Market”. The “Single Market” is as an “*area without internal frontiers in*

¹⁰⁵ Genschel P. & Jachtenfuchs M., *How the European Union constrains the state: Multilevel governance of taxation*, in *European Journal of Political Research* (50), 2011, pp.293-294.

*which the free movement of goods, persons, services and capital is ensured*¹⁰⁶. And since goods, persons, services and capital constitute the major tax bases of Member States, this residual European power to regulate extends to all major taxes. The EU institutions have used this power to progressively assert considerable control: in fact, while Member States continue to levy taxes, EU institutions increasingly shape them¹⁰⁷.

The nexus between taxation and market integration is twofold: on the one hand, substantial differences between national tax laws may constitute important obstacles to the Common Market. Moreover, only a Europe capable of optimizing market conditions within the Common Market will be able to compete on equal terms with the big economies of the rest of the world; and on the other hand, provisions of a discriminatory and restrictive nature in national tax laws may constitute obstacles, for example, because of their differential treatment of residents and non-residents.

Thus, in the field of taxation, integration may be achieved in a positive or in a negative way. Positive integration is achieved by tax harmonization or at least coordination between Member States. This is an integration by way of coordination of national policies, common policy-making, and approximation of national laws. Negative integration, as opposed, is a kind of integration brought on through legally enforceable prohibitions on discriminatory measures and restrictive features of national tax systems¹⁰⁸.

Necessary is to note that the harmonization in the field of indirect taxation has been regulated from the beginning by the European Treaties, at the moment of the constitution of the European Economic Community (1957). In fact, among tax impediments, customs duties and discriminating domestic taxations of foreign goods and services are the most

¹⁰⁶ Treaty on the Functioning of the European Union, Article 26.

¹⁰⁷ Genschel P. & Jachtenfuchs M., *How the European Union constrains the state: Multilevel governance of taxation*, cit., p. 297.

¹⁰⁸ Gribnau H., *Soft Law and Taxation: EU and International Aspects*, cit..

conspicuous ones, and they visibly and directly affect the freedom to trade¹⁰⁹. Consequently, the Community adopted an abundance of secondary laws in the field of indirect taxes.

Direct taxation, as opposed, is scarcely regulated in the Treaties, and this considerably narrower treaty basis has brought to many difficulties in the attempts of harmonizing the national laws on direct taxation. As a consequence of that, far less positive integration has been achieved in direct taxation than in indirect taxation.

The regulatory power of the European Union on tax matters, is exerted through the secondary tax legislation, through the European Court of Justice tax jurisprudence, and through instruments of soft law promoting a method of coordination. As it will be later on explained, this last regulatory mean has become, from the 90's, the main source of tax regulations.

The secondary tax legislation, expression that refers to binding legislative acts of the Council or of the Commission concerning the national tax policy of the Member States, is a tool, aimed to harmonize the national tax regimes, that the EU Treaties give to the EU institutions, but together with strict functional and procedural constraints on them: it can be used solely for ensuring and enhancing the proper functioning of the single market (Articles 113 and 115 TFEU), and the adoption of any act is subject to the unanimity rule (both for the direct and for the indirect taxation) (Articles 113, 114 (2) and 223 (2) TFEU). Notwithstanding this limitations, especially the veto power given to every single Member State from the unanimity rule, the number of secondary tax legislation has constantly increased over the years, and has now become a routine affair in the EU politics.

¹⁰⁹ Terra B.J.M. & Wattel P., *European Tax Law*, Deventer, Kluwer, 2007, p. 91.

Secondary tax legislations acts consist, in practice, in regulations, decisions and, above all, directives. The firsts are acts that impose a uniform discipline for all the Member States and for this reason are not very common in the tax field and their absolute number is still quite low. The decisions are instruments through which the EU usually authorizes specific derogations from general harmonization directive for the Member State addressed by the decision itself. And finally, the directives are undoubtedly the secondary legislation instrument most used in tax matter. As they are binding only with respect to the ends to be achieved, but leave some discretion as to the means by which to achieve them, they allow the national tax systems to adapt gradually to the exigencies of the common market. Besides, directives were the instrument of choice for imposing unity on widely diverging national tax regimes. Indeed, they are still the preferred instrument for major acts of tax harmonisation¹¹⁰.

The tax jurisprudence of the European Court of Justice (ECJ) is another important tool in shaping the domestic tax rules of the Member States.

The ECJ, according to the EU Treaties, is the institution empowered of reviewing the consistency of the national laws with the European rules, and while each tax case formally concerns only a particular tax rule in a particular Member State, the resulting case law has a harmonizing effect across taxes and Member States because, by providing detailed reasons why the particular rule is (not) in line with EU law, it establishes general principles of acceptable tax policy for the EU as a whole¹¹¹.

The tax jurisprudence of the ECJ is driven by two types of proceedings: references for preliminary rulings, and infringement procedures. Preliminary rulings have always outnumbered infringement procedures by a significant margin. Infringement proceedings

¹¹⁰ Genschel P. & Jachtenfuchs M., *How the European Union constrains the state: Multilevel governance of taxation*, cit., p. 299.

¹¹¹ *Ivi*, p. 300.

are almost invariably initiated by the European Commission, that chiefly uses these proceedings to ensure Member States compliance with existing EU law, but also to create new law. By targeting tax obstacles that Member States refuse to remove via legislative harmonisation in the Council, the Commission hopes to trigger case law that removes them through judicial harmonisation¹¹².

Finally, as briefly mentioned above, from the late 90's and progressively more in the last decade, some crucial factors like the financial crisis of the 2008, the obstacles and often the paralysis due to the unanimity rule, the general reluctance of the Member States to delegate fiscal competences to the European Union and the progressive erosion of the national tax bases with the consequent loss of revenues, have brought the EU and the Member States to resort to a kind of regulation, soft and flexible, based on coordination rather than on harmonization. Especially in the field of the direct taxation. Facing the issues of the base erosion and of the profit shifting, both the European Union and the Member States have realized that the best way to safeguard their tax revenue and the tax collection, is through coordination. Not autonomously but together, through integration, coordination, through common principles, and the creation of a tax governance, it is possible to tackle the modern issues of the European taxation.

A system of tax governance is therefore the European answer to the demand of tax rules. Its main feature is the systematic use of a kind of regulatory instruments (soft law) that give the possibility on one hand to operate without the transfer of competences from the Member States to the European Union, and on the other hand to overcome the rigidities of the directives and of the unanimity rule.¹¹³ From the 90's until nowadays, and especially in the last decade after the financial crisis of the 2008, the tax governance has tried to foster a

¹¹² *Ivi*, p. 303.

¹¹³ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 67.

convergence – not an harmonization - of the national fiscal policies of the Member States, through coordination, that is a concept that implies a constant dialogue between EU agencies, various stakeholders and Member States.

Prior to its adoption in the tax field, a method of integration through coordination was already in act in fields like the ones regarding occupational and social policies, and was the so called Open Method Coordination (OMC). The OMC introduced a new kind of govern (more properly, of governance) in specific subjects, pursuing its goals through non-hierarchical instruments, through soft law, through integration through coordination.

What later happened in the taxation field, even if formally without the level of institutionalization proper of the Open Method Coordination¹¹⁴, has undoubtedly drawn inspiration from the OMC itself.

What has developed, indeed, is exactly a governance, soft and flexible, based on coordination rather than on harmonization. Coordination entails the approximation of the national policies towards a unique and collective reality, which describes the complexity and the interdependence of the European society and economy¹¹⁵. The regulatory outcome of coordination are guidelines, programmes, recommendations, communications, codes of conduct or action plans, adopted at a central or at a local level, that are supported by the governments, and periodically subject to revision and peer reviews, that are other very important devices to exert political pressure and to push towards the compliance.

The starting moment of the European tax governance is usually dated back to the 1997, when the ECOFIN Council, *ie*, the meeting of the Finance Ministers of the EU Member

¹¹⁴ Melis G., *Coordinamento fiscale nell' Unione Europea*, in *Enciclopedia del Diritto*, Annali, Giuffrè, 2007, p. 417.

¹¹⁵ Borràs S. & Jacobsson K., *The open method coordination and new governance patterns in the EU*, *Journal of European Public Policy*, 11(2), 2004, pp. 185-208.

States, adopted a comprehensive package to tackle harmful tax competition, the Code of Conduct for Business Taxation¹¹⁶.

With this code of conduct (often referred to as the Monti Code, being the European Commissioner Mario Monti the responsible for the internal market, services, customs and taxation at that time), that some authors consider an example of Open Method Coordination¹¹⁷, the principle of harmful tax competition was introduced. This first important soft law instrument was deemed to be expedient, in the fight against harmful tax competition, because most Member States felt that a directive, therefore a mean of hard law, would have eroded political sovereignty.

Thus, is once again demonstrated how the unanimity rule poses a major obstacle to harmonisation in the field of direct taxes. The introduction of the Code of Conduct for Business Taxation was in fact a reaction to the toilsome process of achieving integration (a limited integration, furthermore). Thus, the Monti Memorandum was instrumental in creating a sense of urgency to increase the coordination of the tax policies of the Member States¹¹⁸.

The Code of Conduct is not legally binding, which is emphasised by its preamble: “*The Code of Conduct is a political commitment and does not affect the Member States’ rights and obligations or the respective spheres of competence of the Member States and the Community resulting from the Treaty*”¹¹⁹. The Code embodies a legislative drafting strategy that makes a substantive advance towards tax coordination. “*By proceeding softly*

¹¹⁶ Council conclusions on the ECOFIN Council meeting on 1 December 1997 concerning taxation policy (98/C 2/01), Annex 1, Resolution of the Council and the representatives of the governments of the Member States, meeting within the Council of 1 December 1997 on a *Code of Conduct for Business Taxation*.

¹¹⁷ Radaelli C.M. & Kraemer U.S., *Modes of Governance in EU Tax Policy*, in Tommel I. & Verdun A. (Eds.), *Innovative Governance in the European Union: The Politics of Multilevel Policymaking*, Boulder (CO-US), Lynne Rienner Publishers, 2008.

¹¹⁸ Gribnau H., *Soft Law and Taxation: EU and International Aspects*, cit., p. 81.

¹¹⁹ Code of Conduct for Business Taxation cit..

where hard approaches have failed, the Code will [has] garnered agreement in principle to coordination, broadly phrased”¹²⁰. The non-binding nature of the Code may be considered a strength rather than a weakness. Indeed, on account of the peer pressure involved, Member States have taken the Code seriously and amended most of their tax measures to comply with it¹²¹.

From this moment on, initiatives like the one of the Monti Code, therefore characterized by the usage of instruments of soft law, by the coordination, and by the role played also by non-governmental subjects, have become progressively more frequent, creating the EU tax governance.

The tax governance is a sort of unitary reaction of the European institutions, through programmed and flexible coordination, that has two fundamental objectives, as explained in the European Commission’s press releases on the Communications of the 2009 and of the 2010¹²². The first objective has an internal relevance, and it is to defend the national tax bases against the international tax evasion and tax avoidance, the aggressive tax planning, the abuse of right and the harmful tax competition, and to help in the fight against money laundering, corruption, criminal organization and the financing of terrorism. The second objective, as opposed, has an external relevance, and consists in the aim to stimulate the good tax governance in third countries through international cooperation, especially in the

¹²⁰ Bratton W.W. & McCahery J.A., *Tax Coordination and Tax Competition in the European Union: Evaluating the Code of Conduct on Business Taxation*, Common Market Law Review (38), 2001, p. 685.

¹²¹ Pinto C., *Tax Competition and EU Law*, Kluwer Law International, The Hague, London/New York, 2003, pp. 205-206; and Kieckhefer B.J., *Harmful Tax Competition in the European Union: Code of Conduct, Countermeasures and EU Law*, Kluwer, Deventer, 2004, p. 51.

¹²² IP/09/650, European Commission, Press Release on Communication: “*Taxation and Good governance: The European Commission propose actions to improve transparency, exchange of information and fair tax competition*”, April 28th 2009. And MEMO/10/146, European Commission, Press Release on Communication: “*Tax and Development: Cooperating with Developing Countries on promoting Good Tax Governance in Tax Matters*”, April 21st 2010.

fields of transparency, exchange of information and the fight against the harmful tax competition¹²³.

To sum all these things up, it can be maintained that in the European Union we have a kind of hybrid or also multilevel tax governance. In fact, we have seen that on the one hand the system is based on the rigid formalities and procedures of the EU legislation, and on the other hand it relies upon forms of regulation soft and flexible. Without leaving apart the above mentioned important contribute of the European Court of Justice to the tax matter with its creative jurisprudence.

In this way, the tax governance is able to achieve both the participation of public structures like the Member States or the EU Institutions, and the involvement of the civil society, so to say private actors and enterprises, with the aim of planning targets and ways of realization, sometimes through hierarchical tools, sometimes, rather more frequently, through participative and voluntary instruments of soft law¹²⁴.

This political will of inclusion, draws a portrait with multiple centres of power, which in turn creates a system of shared competences, core feature of the European tax governance.

4.1 Good tax governance

The reference to certain principles marks the difference between governance and good governance. While the term governance indicates a teleological concept, the good governance regards the specific instruments needed for pursuing the right purposes and in the right way: the common principles. In order to get to a good governance social participation, integrity, transparency, trust, equality and responsibility in the application of

¹²³ Rosebuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 69.

¹²⁴ *Ivi*, p. 68-69.

the rules, are required, but also the refusal of unfair practices like the corruption, the money laundering, the participation or collaboration with crime organization and the financing of the terrorism, is clearly essential¹²⁵.

Across the last decade, the European Institutions, and the European Commission in particular, have progressively delineated the framework of the good tax governance.

The European Commission, in its Communication to the European Council, the European Parliament, and the European Economic and Social Committee, entitled “Promoting Good Governance in Tax Matters” of the 2009¹²⁶, highlighted four elements: first, it acknowledged that the economic and financial crisis was threatening the Member States’ accounts and tax systems, and that an enhanced fiscal cooperation and the adoption of common principles could not be delayed any more (“*With the current financial and economic crisis, national budgets and tax systems are under increased threat and the need for international tax cooperation and common standards (i.e. "good governance in the tax area") has become a regular feature of international discussions.*”); second, it affirmed that some aspects of the globalization have negative implications, putting the States in a more vulnerable position for what concerns tax evasion and tax avoidance (“*Globalisation, or the increasing economic integration of markets that is being driven by rapid technological change and policy liberalisation, is providing great opportunities in the world. [...] But there are also social and economic downsides to globalisation. Countries can, for example, become more vulnerable to economic turmoil, as is evident at present, and to tax avoidance and evasion. In a world where money moves freely, "tax havens", and*

¹²⁵ Chowdury N. & Skarstedt C., *The Principle of Good Governance*, Centre for International Sustainable Development Law, Montreal, 2005. And Weiss F. & Steiner S., *Transparency as an Element of Good Governance in the Practice of the EU and the WTO: Overview and Comparison*, Fordham International Law Journal, 30(5), 2006, pp. 1545-1586.

¹²⁶ COM(2009) 201 final, Commission of the European Communities Communication to the European Council, the European Parliament, and the European Economic and Social Committee, *Promoting Good Governance in Tax Matters*, Brussels, 28.4.2009.

insufficiently regulated international financial centres that refuse to accept the principles of transparency and information exchange can facilitate or even encourage tax fraud and avoidance, negatively affecting the tax sovereignty of other countries and undermining their revenues. [...] With national budgets and, therefore, social and other policies under severe strain this is an extremely serious problem.”); third, it said that it was essential to conclude agreements with States out of the European Union to define common standards and the cooperation on tax matters (“[...] a viable option, therefore, is to manage the effects better by means of agreements with third countries on as broad a geographical basis as possible covering common standards and cooperation, including in tax matters.”); and fourth, it confirmed that the communitarian cooperation within the European Union is an essential instrument to fight properly the tax erosion, being individual or bilateral solutions absolutely insufficient (“[...] individual national and bilateral measures can only partly address tax erosion problems and that EU-wide cooperation is vital. Member States have agreed on several measures which are designed to promote better governance in the tax field within the EU.”).

The year before, the 14th of May 2008, the ECOFIN had already defined the good tax governance on the basis of the principles of transparency, exchange of information and fair tax competition. In a following moment, the principle of corporate social responsibility was added to the previous ones.

By listing these principles, the EU for the first time indicates the common principles that constitute the good tax governance, meaning the principles that, despite being rather wide and requiring a constant process of definition and innovation, specify the characteristics that have to guide the tax system of each Member State¹²⁷.

¹²⁷ Rosebuj T., *I principi e la tax governance nell'Unione Europea*, cit., p. 71.

An accurate determination, once for all, of the content of the principles of good tax governance is not easy though. Or better, is impossible. In fact, due to the unpredictability and perpetual change of the context, and the continuous string of new circumstances, the principles can hardly be described. Nonetheless, it can be given a description of the facts that characterize them, through the accumulation of identification data. However, also adopting this kind of approach, it turns out to be a difficult and not linear process¹²⁸.

After the two aforementioned European acts, the process of evolution of the good tax governance has seen the contribution of several other acts, widening and/or specifying and/or adapting the principles to the contingent changes of the context, also promoting the adoption of the good tax governance in third countries.

Paragraph 5 will give an in depth analysis of the good tax governance principles.

4.2 EU soft law

Before jumping to the description of the principles of the European good tax governance, interesting is to reserve a paragraph to the features of the soft law in the European Union, after having talked about it generally, before, in paragraph 2.

It has already been explained as the soft law is used as an alternative to, or complement of, legislation, and why this happens. With specific reference to the European Union, in order to understand the precise role that certain soft law instruments play, it is useful to offer a classification made on the basis of the function and objective of the various soft law instruments¹²⁹.

¹²⁸ *Ivi*, p. 74.

¹²⁹ Classification taken from: Gribnau H., *Soft Law and Taxation: EU and International Aspects*, cit..

A first category of soft law can be identified in the preparatory and informative instruments. These include, in particular, Green Papers, White Papers, action programmes, and informative communications. These instruments do not indicate any guideline for behaviour. Their goal is just to prepare future Community law and policy and/or to provide information on Community action.

Senden correctly wonders whether these instruments actually constitute soft law at all. In fact, not establishing any rule of conduct, they only pave the way for the adoption of future legislation (the proper rule of conduct) “*in the sense that they are an element in the assessment of their desirability or necessity and possible contents*”¹³⁰. As such, they can also be regarded as fulfilling a real pre-law function, in the sense that they might facilitate the subsequent adoption of legislation by providing or increasing the basis of support for the rules contained therein¹³¹. The Monti Code, for instance, should be mentioned here, in this category of soft law instruments.

The second category Gribnau proposes is the one of the interpretative and decisional soft law devices. This type of instruments are aimed to indicate which has to be the interpretation and the application of existing pieces of law, this way “*enhancing legal certainty, legal equality, and transparency*”¹³². More precisely, while the interpretative devices concern, of course, only the way existing law provisions has to be interpreted, the decisional ones have a further function: they specify in which way a certain EU law will be applied by a European institution, in cases in which it has implementing and discretionary powers.

¹³⁰ Senden L., *Soft Law, Self-regulation and Co-Regulation in European Law: Where Do They Meet?*, 9 Electronic Journal of Comparative Law, www.ejcl.org, 2005.

¹³¹ McLure C.E., *Legislative, Judicial, and Soft Law Approaches to Harmonizing Corporate Income Taxes in the US and the EU*, 14 Columbia Journal of European Law, section 1B and IVE, 2008.

¹³² Gribnau H., *Soft Law and Taxation: EU and International Aspects*, cit., p. 104.

Because of their peculiar function, the decisional soft law instruments can also be said to have a kind of binding power. In fact, on the basis of the principle of legitimate expectations, the EU institution will have to be consistent with the behaviour foretold.

Examples of this second category of European soft law are the Commission's communications and notices and also certain guidelines, codes, and frameworks frequently adopted in the areas of competition law and State aid. For instance, the Communication of the Commission “on the consequences of the judgment of the ECJ in the case *Cassis de Dijon*”^{133,134}, and the Communication from the Commission to the Council, the European Parliament, and the European Economic and Social Committee on “Dividend taxation of individuals in the Internal Market”¹³⁵.

The third and last category of soft law, is constituted by the steering instruments. Their purpose is “*establishing or giving further effect to Community objectives and policy or related policy areas*”¹³⁶. This objective is pursued sometimes through political ways – with acts like declarations and conclusions – and some other times through ways that promote a closer cooperation – it is the case of recommendations, resolutions and codes of conduct. The Code of Conduct for Business Taxation could be taken as example also in this other category.

¹³³ Case 120/78, *Rewe-Zentral AG v Bundesmonopolverwaltung für Branntwein (Cassis de Dijon)*, 1979, ECR 649.

¹³⁴ OJ 1980, C 256/2, Commission of the European Communities, *Communication from the Commission concerning the consequences of the judgment given by the Court of Justice on 20 February 1979, in Case 120/78 (Cassis de Dijon)*.

¹³⁵ COM(2003) 810 final.

¹³⁶ Gribnau H., *Soft Law and Taxation: EU and International Aspects*, cit., p. 105.

5. EU good tax governance principles

It will follow a description of the articulated principles that constitute the European good tax governance.

5.1 Corporate social responsibility

The insertion of the principle of corporate social responsibility among the European principles of good tax governance, can be dated back to 2011, when the Commission released a Communication¹³⁷ whose main point was to stress the importance of the reconnaissance of the responsibility that enterprises have towards the society and the environment, often with ethical and human rights matters entailed.

The Commission put forward a new definition of corporate social responsibility (CSR) as “*the responsibility of enterprises for their impacts on society*”¹³⁸. Indeed, the CSR principle generally related to many different fields, pushes the enterprises to engage close relationships with the various stakeholders, by way of respecting the environment, sharing social and ethical concerns and respecting human and consumer rights. By doing so, they are likely to be able to reach the goal of “*maximising the creation of shared value for their owners/shareholders and for their other stakeholders and society at large*” and “*identifying, preventing and mitigating their possible adverse impacts*”¹³⁹.

The direction in which the corporate social responsibility aims ramify are multiple: they range from the human rights, labour and employment practices (such as training, diversity,

¹³⁷ CE, COM(2011) 681, Commission of the European Communities Communication to the European Council, the European Parliament, the European Economic and Social Committee and the Committee of the Regions, *A renewed EU strategy 2011-14 for Corporate Social Responsibility*, October 25th 2011.

¹³⁸ *Ibid.*

¹³⁹ *Ibid.*

gender equality and employee health and well-being), environmental issues (such as biodiversity, climate change, resource efficiency, life-cycle assessment and pollution prevention), and combating bribery and corruption, to Community involvement and development, integration of disabled persons, and consumer interests, including privacy; from the promotion of social and environmental responsibility through the supply-chain, and the disclosure of non-financial information recognised as important cross-cutting issues, to the enhancement of the good tax governance¹⁴⁰.

In the Communication itself, the Commission affirms as, through the CSR principle, enterprises are encouraged also to work towards the implementation of the three principles of good tax governance – transparency, exchange of information and fair tax competition – and to contribute with their business strategies, to fight against international tax avoidance and the profit shifting to tax heavens.

The widespread activity of the enterprises consisting in making plans and strategies aimed to minimize the tax burden, beyond being a deplorable practice, has a negative impact on the society in general and on the tax governance. For this reason the corporate social responsibility has to be considered as the fourth pillar of good tax governance¹⁴¹.

The CSR, which is a superior, general and common principle, from a fiscal point of view, specifies itself in the middle level principle of the fight against the aggressive tax planning, and tackles the impact that the aggressive tax planning itself has on the society: which is on the one hand, the harm of the fiscal interest of the States and of their right to collect taxes, and on the other hand, the damage of all the other tax payers that are subject to an increase of their tax burden.

¹⁴⁰ *Ibid.*

¹⁴¹ Rosembuj T., *Tax morale*, cit..

The European Commission defines the aggressive tax planning in correlation with the CSR principle by stating that “*some taxpayers may use complex, sometimes artificial, arrangements which have the effect of relocating their tax base to other jurisdictions within or outside the Union. In doing this, taxpayers take advantage of mismatches in national laws to ensure that certain items of income remain untaxed anywhere or to exploit differences in tax rates. By paying taxes businesses can have an important positive impact on the rest of society. Aggressive tax planning could thus be considered contrary to the principles of Corporate Social Responsibility*”¹⁴².

Aggressive tax planning therefore is the core issue related to the corporate social responsibility in tax matter.

More technically, the aggressive tax planning, which is an attribute of the concept of abuse of right, consists in creating complex schemes that, albeit formally complying with the prescriptions of the law, betray their scope and violate the *ratio legis*.

These practices, that can also be called of creative compliance (“*compliance with the letter of the law while totally undermining the policy behind the words*”¹⁴³), are carried out via several methods. For instance: the transfer of intellectual properties from ordinary tax jurisdictions to law or zero tax ones; intra-group debt, through which subsidiaries resident in law or zero tax jurisdictions lend money to the parent resident in ordinary tax jurisdiction in order for it to benefit from the deduction of interests; the tax arbitrage to obtain double deductions; the establishment of residence in tax heavens through societies without any economic substance, etcetera.

¹⁴² EC, COM(2012) 722, Communication from the Commission to the European Parliament and the Council, *An Action Plan to strengthen the fight against tax fraud and tax evasion*.

¹⁴³ McBarnet D., *When Compliance is not the Solution but the Problem: From Changes in Law to Changes in Attitude*, cit., p. 7.

The European institutional position with respect to aggressive tax planning, is contained in the Recommendation issued by the Commission in 2012¹⁴⁴. Here the EC decides to conform to the definition of aggressive tax planning given by the OECD, and indeed it maintains that “*aggressive tax planning consists in taking advantage of the technicalities of a tax system or of mismatches between two or more tax systems for the purpose of reducing tax liability*” and adds that “*a key characteristic of the practices in question is that they reduce tax liability through strictly legal arrangements which however contradict the intent of the law*”¹⁴⁵.

The Recommendation also suggests, in order to recognize and fight aggressive tax planning, to check for the possible artificiality of the arrangement and, in this regard, specifies that “*an arrangement or a series of arrangements is artificial where it lacks commercial substance*”¹⁴⁶. For carrying out this evaluation, the Commission advises Member States to check whether the suspect arrangement involves: “*(a) the legal characterisation of the individual steps which an arrangement consists of is inconsistent with the legal substance of the arrangement as a whole; (b) the arrangement or series of arrangements is carried out in a manner which would not ordinarily be employed in what is expected to be a reasonable business conduct; (c) the arrangement or series of arrangements includes elements which have the effect of offsetting or cancelling each other; (d) transactions concluded are circular in nature; (e) the arrangement or series of arrangements results in a significant tax benefit but this is not reflected in the business risks undertaken by the taxpayer or its cash flows; (f) the expected pre-tax profit is insignificant in comparison to the amount of the expected tax benefit*”¹⁴⁷.

¹⁴⁴ EC, C(2012) 8806, European Recommendation of 6.12.12 on *Aggressive tax planning*.

¹⁴⁵ *Ibid.*

¹⁴⁶ *Ibid.*

¹⁴⁷ *Ibid.*

Then, the Recommendation says that “*the purpose of an arrangement or series of arrangements consists in avoiding taxation where, regardless of any subjective intentions of the taxpayer, it defeats the object, spirit and purpose of the tax provisions that would otherwise apply*”¹⁴⁸. This is a key point in the act. Indeed it clarifies as the Commission, regarding the aggressive tax planning, overlooks any kind of “*subjective intention of the tax payer*”¹⁴⁹.

Therefore the Commission, in conformity with the OECD¹⁵⁰, focuses exclusively on the objective aspect of the formal compliance with the letter of the law and the substantial violation of it, without taking into consideration any subjective implication of the matter.

However, many scholars, for instance Doreen McBarnet¹⁵¹ and Tulio Rosembuj¹⁵², claim that the aggressive tax planning is necessary made up of two elements: the objective one, recognized by the Commission, and a subjective one. This second requisite basically consists in the intention of the tax payer of gaining an advantage through the creation of innovative schemes able to overcome the *ratio legis*, in his will of behave this way. And it has to be present in order to have a case of abuse of right.

Thence, moving from this idea, to which I find myself in accordance, the Commission’s legal framework of the aggressive tax planning has to be considered seriously incomplete.

A first weak point emerges when the recommendation defines the aggressive tax planning as “*strictly legal arrangements*”¹⁵³. That could have been acceptable if only the objective circumstances were taken into account. But from a wiser point of view, considering also the subjective side, it is not possible to consider the exploitation of the letter of the law to

¹⁴⁸ *Ibid.*

¹⁴⁹ *Ibid.*

¹⁵⁰ OECD, *Study into the Role of Tax Intermediaries*, OECD Publishing, Paris, 2008.

¹⁵¹ McBarnet D., *When Compliance is not the Solution but the Problem: From Changes in Law to Changes in Attitude*, cit..

¹⁵² Rosembuj T., *Minimizaci3n del impuesto y responsabilidad social corporativa*, cit..

¹⁵³ EC, C(2012) 8806, cit..

artificially gain a fiscal advantage otherwise not obtainable, equal to a real compliance with the law. Even if the provision is formally respected. Moreover, that same result could not have been achieved without a specific mind-set towards the law, because no abuse of right can occur unintentionally.

There cannot be any aggressive tax planning or any abuse of right that are unwanted or without a plan of arrangements¹⁵⁴.

A contradiction of the same type can be noticed in the Recommendation when, talking about the countermeasures that Member States are advised to take in order to face the aggressive tax planning, it says “*in determining whether an arrangement or series of arrangements has led to a tax benefit [...], national authorities are invited to compare the amount of tax due by a taxpayer, having regard to those arrangement(s), with the amount that the same taxpayer would owe under the same circumstances in the absence of the arrangement(s)*”¹⁵⁵. Also here, through referring to “arrangements”, it indirectly admits that the minimization of the tax burden cannot occur without a subjective input of intentionality.

Excluding the subjective circumstances has also an additional implication: the Commission proposes as a tool to tackle more efficiently the abuse of right, the collective adoption of a general anti-abuse rule (“*To counteract aggressive tax planning practices which fall outside the scope of their specific anti-avoidance rules, Member States should adopt a general anti-abuse rule, adapted to domestic and cross-border situations confined to the Union and situations involving third countries*”¹⁵⁶). And the consequence that would derive from the fact that the anti-abuse clause do not consider the parameter of intentionality would be that, in case of an abuse, it would bring to the rectification (redefinition of the

¹⁵⁴ Rosebuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 85.

¹⁵⁵ EC, C(2012) 8806, cit..

¹⁵⁶ *Ibid.*

transaction in compliance to what should have been paid without the arrangement) instead of the sanction. This way loosing lot of its power.

A strict regard solely of the objective circumstances, would bring the abuse of right, concrete effect of the aggressive tax planning, to be considered a perfectly legal instrument. But the reality is that the abuse of right, cannot be at the same time in accordance and in contrast with the law. In fact, when a behaviour or an arrangement is contrary to the common principles, of moral level, external and superior, its legitimacy cannot be determined just through the literal expression of the law¹⁵⁷. Other parameters are required. And once again it is fundamental to bear in mind what has been said in chapter I about the importance of the principles as means to interpret and apply the law flexibly, efficiently and correctly.

The principles bring with themselves superior evaluation criteria that allow to give a definite sense to the laws and to the illicit acts.

With reference to the interesting approach proposed by Atienza and Ruiz Manero¹⁵⁸, the illicit acts are claimed to be, in general, the acts contrary to the rules or to the principles: there can be typical illicit acts – the ones contrary to the rules – or atypical illicit acts – the ones contrary to the principles. In this latter category, we can find the illicit acts that divert the meaning and the sense of a law. This happens when the letter of a rule permits a conduct, but that same conduct, since it contrasts with one or more principles, from licit turns into illicit. And that is exactly what happens in the case of the abuse of right and the tax avoidance through aggressive tax planning¹⁵⁹.

¹⁵⁷ Perelman C., *Logica giuridica: nuova retorica*, Vol. 39, Giuffrè, Milano, 1979.

¹⁵⁸ Atienza M. & Ruiz Manero J., *Illicitos atípicos. Sobre el abuso del derecho, el fraude de ley y la desviación de poder*, Editorial Trotta SA, Madrid, 2000.

¹⁵⁹ *Ibid.*

Tulio Rosembuj, despite agreeing in general terms with the portrait of the situation proposed by Atienza and Ruiz Manero, makes two important critics to their idea¹⁶⁰: first, he claims that from this theory does not emerge clearly, so it is necessary to explicitly restate it, that the principle on the one hand abolishes the efficacy of the rule in force, and on the other hand, and at the same time, it creates a new rule. Therefore it has an own genetic function; and second, while the Spanish authors, in order to check for the distortion of the law, look only at the damage occurred to third parties without considering the intentionality, Rosembuj reaffirms that the damage is (and has to be) consequence of the will of causing it: only this, he says, is an illicit¹⁶¹.

Ultimately, it is possible to affirm that the existence and the consideration of a common principle, allows to shift from a view of the aggressive tax planning as a legal practice, to a view of it as purely illegal. And this shift occurs when two elements are found together in the practice observed: the damage caused to third parties, and the consciousness of the taxpayer of the harmful nature of its behaviour¹⁶².

Hence, in the matter of the abuse of right, we see on the one hand the objective violation of the law, of its ratio, through the contrast with the principle/s on which the provision rests upon; and on the other hand the indispensable presence of the intention of the tax payer of achieving that illicit tax reduction, so of a “*mental state of consciousness of wrongdoing*”¹⁶³.

Notwithstanding all these reflections, as already mentioned, the Recommendation’s approach to the aggressive tax planning, is characterized, in line with the OECD’s one, by the consideration of the sole objective element, and this inevitably finishes to deeply harm

¹⁶⁰ Rosembuj T., *I principi e la tax governance nell’Unione Europea*, cit., p. 89, and Rosembuj T., *Minimizaci3n del impuesto y responsabilidad social corporativa*, cit..

¹⁶¹ *Ibid.*

¹⁶² Rosembuj T., *Tax morale*, cit..

¹⁶³ Buell S.W., *Good Faith and Law Evasion*, UCLA Law Review, 58, 611-667.

the social corporate responsibility principle, altering the correct sequence of principles. This way, indeed, the aggressive tax planning and the abuse of right are transformed into evaluative standards and inserted in the provisions, therefore becoming parameters of subsumption, rather than principles to be pondered.

Such approach brings with itself that, in spite of the fact that the purpose of the law is totally betrayed by the arrangements constituting the abuse of right, there is not the conception of the atypical illicit acts, and, as a consequence, the corporate social responsibility principle fails to prevail over the illicit behaviour of the taxpayer.

However, the European attitude towards the aggressive tax planning seems to change in the Directive 1164 of the 2016¹⁶⁴ where it commands the creation of a general anti abuse rule, from the description of whom emerges the acknowledge of the necessary presence of a subjective element (see 5.3).

Here is reported a simple scheme taken from “*I principi e la tax governance nell’ Unione Europea*”, by Tulio Rosembuj¹⁶⁵, that gives a concrete example of the hierarchical relation of the principles as discussed in chapter I:

COMMON PRINCIPLE	Corporate social responsibility
MIDDLE LEVEL PRINCIPLE	Aggressive tax planning
EVALUATIVE STANDARD	General anti-abuse clause

¹⁶⁴ 2016/1164/EU, Council Directive, *Laying down rules against tax avoidance practices that directly affect the functioning of the internal market*, July 12th 2016.

¹⁶⁵ Rosembuj T., *I principi e la tax governance nell’ Unione Europea*, cit., p. 135.

5.2 Transparency

With a communication of march 2015 “*on tax transparency to fight tax evasion and avoidance*”¹⁶⁶, the European Commission presented a “*Tax Transparency Package*”, containing a series of measures and of proposals to be adopted by the EU and the Member States in order to address the most urgent issues in this field.

At first, the Communication enlists the results that had been achieved at the EU level in fighting the tax fraud and enhancing transparency and cooperation in tax matters between the Member States. And in this regard, it mentions: the wide and positive effect of the Code of Conduct in Business Taxation to tackle the harmful tax competition and safeguard the good tax governance principles in the Internal Market; the revision of the Directive on Administrative Cooperation, adopted by the Council in December 2014 that allowed the EU to have “*a solid legislative framework for the automatic exchange of information*”¹⁶⁷ and to eliminate once for all the bank secrecy for tax purposes in the EU; the tax agreements signed with Switzerland, Andorra, Monaco, San Marino and Lichtenstein; the implementation of some practical initiatives to facilitate tax transparency, such as standard forms for exchange of information; the fourth Anti-Money Laundering Directive, and other measure.

Then, the Communication focuses on the proposals to further increase transparency in tax matters and to fight tax evasion and avoidance, and it introduces for the first time a crucial concept, that later on will become a key point in the OECD’s BEPS Action Plan, that is the

¹⁶⁶ EC COM(2015) 136, *Communication from the Commission to the European Parliament and the Council on tax transparency and to fight tax evasion and avoidance*, March 18th 2015.

¹⁶⁷ *Ibid.*

goal of assuring that taxation reflects where economic activity takes place. So to say, to “ensure the link between taxation and the place of real economic activity”¹⁶⁸.

The proposals, that constitutes the “Tax Transparency Package” are:

- regarding tax rulings, since they constitutes instruments “used to offer selective tax advantages or to artificially shift profits to low or no tax locations”¹⁶⁹ and since there is now little information exchange between national authorities, the Commission strongly encourage an automatic and periodical exchange of information between Member States on cross-border tax rulings. What’s more, “where relevant, Member States that receive this information can then request more details”¹⁷⁰. And the proposal of the Commission “that these new requirements be built into the existing legislative framework for information exchange, through amendments to the Directive on Administrative Cooperation”¹⁷¹ was turned into practice with the Directive of the December 8th 2015 with which the European Council emended the previous one.
- The extension of the transparency requirements currently existing only for banks and in some aspects for large extractive and logging industries, regarding the detailed report of their annual activities separated for each country in which they operate (country-by-country reporting), to all the multinational companies. “However” specifies the Commission in the act, “the objectives and scope of any such possible initiative would need to be calibrated very carefully”¹⁷².
- The revision of the Code of Conduct for Business Taxation. Albeit it has demonstrated its extremely usefulness, it now needs a review in order to keep its

¹⁶⁸ *Ibid.*

¹⁶⁹ *Ibid.*

¹⁷⁰ *Ibid.*

¹⁷¹ *Ibid.*

¹⁷² *Ibid.*

effectiveness in tackling the harmful tax competition properly, also considering the new practices, for example the use by the Member States of tax incentives such as the patent box. *“Tackling complex new challenges to fair taxation and safeguarding tax transparency requires more decisive action by the Code [...]”*¹⁷³.

- A better quantification of the tax gap. The tax gap is *“the difference between tax that is due and the amount actually collected by national authorities. Tax evasion and avoidance are not the only contributors to the tax gap, with other factors such as administrative errors and bankruptcies also playing a role”*¹⁷⁴. The importance of a better qualification of the tax gap stays in that it is *“an important indicator of the scale of wilful non-compliance in taxation”*¹⁷⁵.
- To promote greater tax transparency internationally. The EU must *“push for an ambitious new international tax framework”*¹⁷⁶ and it is evident as *“greater financial transparency and fairness is a key area for our partner countries to achieve their development objectives and implement the post 2015 global development agenda”*¹⁷⁷.

Following to this Communication, the European Commission, in June, issued another Communication, trying to set out a more comprehensive European approach to corporate taxation¹⁷⁸. This act, entitled *“A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action”*, widens the perspective on transparency measures and it is aimed to create a different and more efficient corporate tax system within the European Union. A new approach able to ensure that corporate taxation is fair and transparent, but at

¹⁷³ *Ibid.*

¹⁷⁴ *Ibid.*

¹⁷⁵ *Ibid.*

¹⁷⁶ *Ibid.*

¹⁷⁷ *Ibid.*

¹⁷⁸ EC, COM(2015) 302, Communication from the Commission to the European Parliament and the Council, *A Fair and Efficient Corporate Tax System in the European Union: 5 Key Areas for Action*, June 17th 2015.

the same time growth-friendly, is pursued. The current issues, essentially due to the globalization of the economic environment, often make difficult to ascertain which country has the right to tax an enterprise or specific operations, and *“certain companies are exploiting this situation to artificially shift profits to the lowest tax jurisdictions and minimise their overall tax contribution”*¹⁷⁹. This unfair situation is likely to affect not only merely the tax revenue of the States but, at the basis, the entire functioning of the system, with the citizen not feeling any more a sense of equity and possibly renounce to comply with their fiscal duties. An alteration of the tax morale. (*“The fact that certain profitable multinationals appear to pay very little tax in relation to their income, while many citizens are heavily impacted by fiscal adjustment efforts, has caused public discontent. This perceived lack of fairness threatens the social contract between governments and their citizens, and may even impact overall tax compliance. There is an urgent need to challenge such corporate tax abuse and to review corporate tax rules in order to better tackle aggressive tax planning”*¹⁸⁰).

The identified five key areas for intervention are: creating a common consolidated corporate tax base (CCCTB); ensuring an effective taxation where the profits are generated; additional measures for a better tax environment for business; further progresses on tax transparency; enhancing the functioning of coordination tools in the EU.

First point: the common consolidated corporate tax base (CCCTB) would allow the cross-border groups to consolidate their tax base and unify the report of their activities in the EU in a unique declaration, offsetting losses in one Member State against profits in another. This measure would strongly reduce the complexities and the costs for the multinational enterprises that would only have to follow one set of rules when computing their taxable

¹⁷⁹ *Ibid.*

¹⁸⁰ *Ibid.*

income. Besides, *“the CCCTB could be highly effective in tackling profit shifting and corporate tax abuse in the EU”*¹⁸¹, especially through the elimination of the possibility of exploit the mismatches between the tax systems and to manipulate the transfer pricing. The Commission also affirms its commitment to work on a proposal *“to make the CCCTB compulsory, at least for multinational enterprises”*¹⁸².

Second point: to guarantee that the revenue is taxed where the economic activity effectively takes place (*“Companies that benefit from the Single Market and generate profits there should pay tax on those profits within the EU, at the place of activity”*¹⁸³). The practice of the enterprises of shifting their profits to countries with low or zero tax rate, with no link to where the value is created has to be fought adjusting the definition of “permanent establishment”, *“so that companies cannot artificially avoid having a taxable presence in Member States in which they have economic activity”*¹⁸⁴ and enhancing the Controlled Foreign Corporations (CFC) rules, *“which ensure that profits parked in low or no tax countries are effectively taxed”*¹⁸⁵. In addition, the EU will have to pay attention to the fact that the EU corporate tax legislation aimed at preventing double taxation does not inadvertently lead to double non-taxation. Indeed, *“it should amend the legislation so that Member States are not required to give beneficial treatment to interest and royalty payments if there is no effective taxation elsewhere in the EU”*¹⁸⁶.

Third point: to create a better environment and encourage business. While the measures regarding CCCTB are implemented and double taxation dispute resolution mechanism are

¹⁸¹ *Ibid.*

¹⁸² *Ibid.*

¹⁸³ *Ibid.*

¹⁸⁴ *Ibid.*

¹⁸⁵ *Ibid.*

¹⁸⁶ *Ibid.*

improved, the EU should focus on giving the possibility to group entities to offset profits and losses they make in different Member States.

Fourth point: further progression on tax transparency. In order to move towards this objective, the Commission suggests and confirms the importance of the automatic exchange of information on cross-border tax rulings and of the implementation of the BEPS Action Plan. In addition, it claims that, in order to boost transparency, Member States should compare their national black-list of non-cooperative tax jurisdiction with the one published by the EU. *“The list, published on the Commission's website, offers Member States a transparent tool to compare their national lists and adjust their respective approaches to non-cooperative tax jurisdictions as necessary”*¹⁸⁷. And lastly, the Communication announces that other information duties for the enterprises will add to the country-by-country report existing ones.

Fifth point: an improvement and a better exploitation of the coordination and of the cooperation between the EU Member States is strongly recommended. In particular, is claimed the necessity of a revision of the Code of Conduct for Business Taxation and of the implementation of non-legislative measures against tax avoidance.

Then again, in 2016, in another Communication¹⁸⁸, the European Commission underlined three priorities: the transparency, the assurance that all the companies operating in the EU pay their taxes where profits and value are generated, and the promotion of good tax governance globally. Moreover the Commission states that the concept of legal certainty has become a new global focus, after being recognized by the G20, and that it has to accompany the other principles of good tax governance, creating *“a balance between implementing necessary reforms and providing a steady, clear and predictable tax*

¹⁸⁷ *Ibid.*

¹⁸⁸ EC, COM(2016) 682, Communication from the Commission to the European Parliament and the Council, *Building a fair, competitive and stable corporate tax system for the EU*, October 25th 2016.

environment for businesses”¹⁸⁹. But above all, this Communication reaffirms and specifies the improvements that the adoption of the outlined CCCTB would bring, especially for the fact that through the CCCTB the anti-abuse and anti-tax arbitrage clauses protecting the States against the base erosion and the profit shifting would be adopted, and at the same time the CCCTB would sustain the deduction of the costs of research and development, allowing to reward the enterprises really, and not fictitiously, investing in that kind of activities.

Third and last relevant European provision to be mentioned in the matter of tax transparency, is the Communication of July the 5th 2016 entitled “*Communication on further measures to enhance transparency and the fight against tax evasion and avoidance*”¹⁹⁰.

5.2.1 Enhanced transparency

After having reaffirmed the importance of fighting the different forms of tax abuse in order to avoid the tax burden to result proportionally heavier on small and medium enterprises and on physical persons than on big multinationals, threatening the delicate balance of the social contract, the Commission puts forth other initiatives to face the priority areas for action. The overall direction of these proposals is in the sense of an enhanced transparency, to give the possibility to check and control the fairness of the behaviour of the tax payer. To pursue the goal of an enhanced transparency, three figures are fundamental: the beneficial owner, the enablers and promoters of the aggressive tax planning, and the whistle blower.

¹⁸⁹ *Ibid.*

¹⁹⁰ EC, COM(2016) 451, Communication from the Commission to the European Parliament and the Council, *Communication on further measures to enhance transparency and the fight against tax evasion and avoidance*, July 5th 2016.

I. The EU has adopted the figure of the beneficial owner emerging from the FATF Recommendations and from the G20, in which the beneficial owner is defined as “*the natural person(s) who ultimately owns or controls a customer and/or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement*”¹⁹¹. In order to fight the money laundering, the corruption, the financing of the terrorism and the tax frauds, the figure of the beneficial owner, that usually hides behind the misuse of corporate vehicles, is crucial.

That is the reason why the Communication suggests to create common and public registers of beneficial owners for the whole EU, to oblige Member States to share their national lists of beneficial owners, and to publish these information. Indeed, allowing tax authorities to direct access to the detailed beneficial ownership information of other Member States, even apart from the anti-money laundering and financing of terrorism purposes, would significantly improve their ability to target risks of tax evasion and avoidance. This mechanism would turn the information on beneficial ownership collected about the money laundering, in information to individuate and fight fiscal crimes.

The Communication goes on saying that at EU level, all the Member States have agreed to participate in a pilot project, launched by UK, Germany, Spain, Italy and France, to exchange information on the ultimate beneficial owners of companies and trusts¹⁹², and that this would be a natural extension of the transparency provisions already enshrined in EU law and of the proposals presented in the

¹⁹¹ The FATF Recommendation, *International standards on combating money laundering and the financing of terrorism & proliferation*.

¹⁹² <http://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Taxation/Articles/G5-letter-to-G20-counterparts-regarding-action-on-beneficial-ownership.html>.

Communication itself which allow tax authorities full access to beneficial ownership information. *“The automatic exchange of information on beneficial ownership could potentially be integrated into the binding tax transparency framework already in place in the EU”*¹⁹³.

- II. The enablers and the promoters of the aggressive tax planning are tax advisors, legal advisors or financial institutions that actively help their clients to make use of aggressive tax planning arrangements in order to reduce the tax burden and to conceal money offshore. They also organize and manage the commercialization of this tax avoidance arrangements.

Member States at the informal ECOFIN Council of April 2016¹⁹⁴ invited the Commission to consider initiatives on mandatory disclosure rules inspired by the OECD/G20 Base Erosion and Profit Shifting (BEPS)¹⁹⁵ Action 12, with regard to introducing more effective disincentives for intermediaries who assist in tax evasion schemes. The BEPS Action 12, indeed, recommend the introduction of a mandatory disclosure regime requiring tax payers and promoters of tax planning schemes to disclose any aggressive tax planning arrangement that they use or promote. And it is exactly in the direction of an increased transparency and access to the right information at an early stage that the EU wants to move, allowing *“the authorities to improve the speed and accuracy of their risk assessment and make timely and informed decisions on how to protect their tax revenues”*¹⁹⁶. This disclosure of information, proposed by the Commission in the Communication of

¹⁹³ EC, COM(2016) 451, cit..

¹⁹⁴ Informal ECOFIN Council of 22 April 2016.

¹⁹⁵ OECD/G20 Base erosion and profit shifting –BEPS (2015).

¹⁹⁶ EC, COM(2017) 335 final, *Proposal for a Council Directive amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements*, June 21th 2017.

June 2017¹⁹⁷, should enable tax authorities to track the arrangements and respond to the tax risks that they pose by taking appropriate measures to curb them, and also to have a deterrent effect. The instrument proposed is rather ambitious: it is based on an upgrade of the automatic exchange of information and on a combined attack to the various elements that constitute the tax avoidance (tax arbitrage, harmful tax competition, transfer price), and the information exchanged, besides being a new channel of communication between Member States, would also include the instruments of an only potentially aggressive tax planning¹⁹⁸. The obligation, however, concerns only cross-border situation.

Another key point in the proposal is the timing of the disclosure. The envisaged deterrent effect and the evaluation of the risks that the mechanism brings, are more likely to be achieved if the disclosure is made early on, before the scheme is actually implemented. That is why the Communication recommends that intermediaries “*disclose the reportable arrangements within 5 days beginning on the day after such arrangements become available to a taxpayer for implementation*”¹⁹⁹. Member States then have a wide discretion in determine the sanction to be applied.

The Commission, because of the adoption of the exchange of information method and especially because of the fact that “*aggressive tax planning structures have evolved over the years to become particularly complex and are always subject to constant modifications and adjustments to react to defensive counter-measures by the tax authorities*”²⁰⁰, have decided not to give a definition of aggressive tax

¹⁹⁷ *Ibid.*

¹⁹⁸ *Ibid.*

¹⁹⁹ *Ibid.*

²⁰⁰ *Ibid.*

planning, but to resort to hallmarks, a compilation of the features and elements of transactions that present a strong indication of tax avoidance or abuse. And “*it suffices that an arrangement fall within the scope of one of those to be treated as reportable to the tax authorities*”²⁰¹.

There are general and specific hallmarks that will serve as indicators rendering a cross-border arrangement reportable insofar as they meet the main benefit test, which states that the main benefit for setting up a structure is to obtain a tax advantage. And these hallmarks are: the intermediary receives a fee for its services proportionate to the amount of the tax advantage; taxpayer is under the obligation not to disclose how such arrangement can secure a tax advantage vis-à-vis other intermediaries or the tax authorities; mass-marketed schemes are used; the use of losses to reduce tax liability. In addition, specific hallmarks related to cross-border transactions, transfer pricing and automatic exchange of information, which do not need to comply with the main benefits test, are included in the proposal.

III. A whistle-blower is defined in the Communication to the Commission of 2012²⁰², as “*a member of staff, acting in good faith, who reports facts discovered in the course of or in connection with his or her duties which point to the existence of serious irregularities*”²⁰³.

The European Commission in the Communication of 2016²⁰⁴ expresses its concern about the necessity of the development of a European common discipline able to protect whistle-blowers and also to incentivize their denounces, maybe through the prevision of an economic reward. The role of whistle blowers and of the rules

²⁰¹ *Ibid.*

²⁰² SEC(2012) 679 final, Communication to the Commission, *Communication from Vice-President Šefčovič to the Commission on Guidelines on Whistleblowing*, December 6th 2012.

²⁰³ *Ibid.*

²⁰⁴ EC, COM(2016) 451, cit..

protecting them, in the context of the enhancement of the transparency rules that the Communication addresses, is recognized as crucial, especially after the recent high-profile cases exposed by whistle-blowers (LuxLeaks) that, if on the one hand have led to the discovery of important irregularities, tax frauds or, more generally, serious threats to the public interest, on the other hand have shown the necessity of deep improvement in the matter.

Any staff member who reports a serious irregularity, provided that this is done in good faith, shall be protected against any acts of retaliation. Indeed, *“the Protection of those who report or disclose information on acts and omissions that represent a serious threat or harm to the public interest does not only enhance employees’ ability to impart such information but has also the potential to crucially contribute to increased detection of fraud and tax evasion, which deprives European tax authorities from legitimate tax revenue”*²⁰⁵. Widen the regulatory frame of the protection of the whistle-blowers and encourage their report, would surely enhance the transparency and therefore allow to make relevant steps forward in the fight against the tax frauds.

The six fundamental points that would become the shared whistle-blower protection criteria are: the protection of the informer from work or retribution related retaliation; safeguard the freedom of expression; grant the confidentiality of identity, the immunity from the violation of the professional secrecy, the protection in case of denounce for defamation or calumny; the possibility of denounce to independent agencies, representative institutions or mass media; the right of

²⁰⁵ *Ibid.*

defence; the possibility to stimulate the interest to denounce through the prevision of rewards.

Scheme about the transparency principle²⁰⁶:

COMMON PRINCIPLE	Transparency/Enhanced transparency
MIDDLE LEVEL PRINCIPLE	<ul style="list-style-type: none"> • Quantification of the tax gap • Beneficial owner • Enablers and promoters of the aggressive tax planning • Protection of whistle-blower
EVALUATIVE STANDARD	<ul style="list-style-type: none"> • Common consolidated corporate tax base (CCCTB) • Transparency of certain enterprises • Country by country reporting

5.3 Protection of the internal market and of the tax base

With reference to this good tax governance principle, the EU relevant act to refer to is the Directive of July the 12th 2016 number 1164²⁰⁷. In this legislative act, the European Union puts forward a corpus of rules aimed at contrasting the practices of tax evasion

²⁰⁶ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 136.

²⁰⁷ 2016/1164/EU, cit..

affecting the functioning of the internal market. In order to do that, the Council decides for the immediate and mandatory implementation by the Member States of the OECD/G20' Base Erosion and Profit Shifting (BEPS)²⁰⁸ Principles in their national tax systems, in the form of evaluative standards.

Trying to build a common legal framework across the EU Countries is the right answer to the need for a common strategic approach and coordinated action, to improve the functioning of the internal market and maximise the positive effects of the initiatives against BEPS. Furthermore, only a common framework could prevent a fragmentation of the market and put an end to currently existing mismatches and market distortions. Nevertheless, the Council limits its action to the compulsory establishment only of minimum levels of protection for the internal market, leaving the detailed implementation to Member States as they are better placed to shape the specific elements of those rules in a way that fits best their corporate tax systems. Article 3 indeed clarifies that “*this Directive shall not preclude the application of domestic or agreement-based provisions aimed at safeguarding a higher level of protection for domestic corporate tax bases*”²⁰⁹.

Thence, some transnational principles of the BEPS Project are made compulsory through the EU legislation, and this mainly thanks to a dominant BEPS general principle that is the right of every country to protect its tax base from its erosion and from the profit shifting and to grant the imposition of the corporate income in the place in which the economic activities really take place and where the added value is created.

In the Article 1, the Directive specifies that the provisions apply to all the tax payers subject to the corporate tax among one or more EU Countries, included permanent establishments in one or more Member States of non EU entities.

²⁰⁸ OECD/G20 Base erosion and profit shifting –BEPS, cit..

²⁰⁹ 2016/1164/EU, cit..

The principles considered by this legislative act are: the interest limitation rule, the controlled foreign companies rule, and the hybrid mismatch arrangements. Furthermore, the Directive adds two more principles not belonging to any of the BEPS Actions, so specific of the EU: the exit taxation and the general anti abuse rule.

- The interest limitation rule: *“Exceeding borrowing costs shall be deductible in the tax period in which they are incurred only up to 30 percent of the taxpayer's earnings before interest, tax, depreciation and amortisation (EBITDA)”*²¹⁰.

The ratio of this rule stays in that through the creation of financial expenses within a transnational group, it is possible to shift profit from one country to another. The deductibility of the interest brings enterprises to put in place strategies of minimization of the tax burden through the payment of an excessive amount of interests for loans received from subsidiaries or branches resident in low or zero tax countries.

What is limited is the deductibility of the exceeding borrowing costs, so the amount of borrowing costs of a taxpayer that exceed taxable interest revenues and other economically equivalent taxable revenues that the taxpayer receives. And the Directive claims the deductibility of up to 30 percent of the EBITDA.

In case of groups that file statutory consolidated accounts, the *“indebtedness of the overall group at worldwide level may be considered for the purpose of granting taxpayers entitlement to deduct higher amounts of exceeding borrowing costs”*²¹¹.

Member States, consistently with the general purpose of the Directive of laying down only minimum standards, are free to establish higher levels of protection or to

²¹⁰ *Ivi*, Article 1.

²¹¹ 2016/1164/EU, cit..

shape differently the details of this rule. For instance, for what concerns the possibility of decrease the percentage, provide for a safe harbour rule so that net interest is always deductible up to a fixed amount when this leads to a higher deduction than the EBITDA-based ratio, place time limits, or restrict the amount of unrelieved borrowing costs that can be carried forward or back. Moreover, Member States can also provide for “*targeted rules against intra-group debt financing, in particular thin capitalisation rules*”²¹².

- The control foreign company rules have their origin in the need to prevent the exploitation of tax heavens through the creation of companies destined solely to the accumulation of non-taxed income and to the deferral of the tax payment in the State of residence of the parent company. The CFC rules basically prevent the parent company from diverting the profits to subsidiaries resident in low or zero tax jurisdictions and not carrying on substantial economic activities²¹³.

According to Articles 7 and 8 of the Directive, “*the Member State of a taxpayer shall treat an entity, or a permanent establishment of which the profits are not subject to tax or are exempt from tax in that Member State, as a controlled foreign company*”²¹⁴ when the parent company holds more than 50% of the voting rights, of its capital, or has the right to receive more than 50% of its profit, and the subsidiary is subject to a tax rate of the 40% lower than the one to which is subject the parent company in its State of residence. If these conditions are met, the effect of the application of the CFC rule is that the subsidiary is treated like a controlled foreign company and consequently the income of the low-taxed controlled subsidiary not

²¹² *Ibid.*

²¹³ Rosebuj T., *Derecho Fiscal Internacional*, El Fisco, Barcelona, 2001.

²¹⁴ 2016/1164/EU, cit..

carrying on any substantial economic activity is re-attributed to its parent company. Then, the parent company becomes taxable on this attributed income in the State where it is resident for tax purposes.

To comply with the fundamental freedoms, such as the freedom of establishment, the CFC rule has to be applied, within the European Union, only in cases where the controlled foreign company is an artificial entity put on with the purpose of gaining tax advantage and does not carry on a substantive economic activity.

Aspects of discretion are left to the Member States here as well.

- With the term hybrid mismatch, or tax arbitrage, is described the practice of the exploitation of the differences and of the discordances between fiscal systems of distinct States to get a tax advantage. The outcome of these kind of harmful practices, unfortunately very common especially after the financial crisis of 2008, is the creation of the so called stateless income, that is an income subject to a double deduction in both States or to a deduction in one of the two States without inclusion in the other: an income non taxed in any part of the world²¹⁵.

Hybrid mismatches are the consequence of differences in the legal characterisation and definition of hybrid instruments, financial instruments with the features of both equity and debt, and of hybrid entities, structures sometimes subject to separate taxation and sometimes to the tax transparency regime. And those differences surface in the interaction between the legal systems of two jurisdictions, and are exploited through practices of tax avoidance.

The result of these arrangements can be either a double deduction, so a deduction of the same payment, expenses or losses occurring both in the Member State in

²¹⁵ Rosembuj T., *La crisis financiera y el arbitraje fiscal internacional*, El Fisco, Barcelona, 2011.

which the payment has its source, the expenses are incurred or the losses are suffered and in another Member State; or a deduction without inclusion, that is the deduction of a payment in the Member State in which the payment has its source without a corresponding inclusion for tax purposes of the same payment in the other Member State²¹⁶.

The strategy recommended by the Directive to tackle the tax arbitrage is: “1. To the extent that a hybrid mismatch results in a double deduction, the deduction shall be given only in the Member State where such payment has its source. 2. To the extent that a hybrid mismatch results in a deduction without inclusion, the Member State of the payer shall deny the deduction of such payment”²¹⁷.

This provisions inevitably imply a wider evaluation from the State, that is required to check for the legal situation existing outside of its borders, in another State, in order to contrast the double non imposition²¹⁸.

- The reason for establishing an exit tax is to avoid that, where the taxpayer decides to move his tax residence or his assets out of the tax jurisdiction of a Member State, the capital gains created in that State, even if not yet realized, remain untaxed.

Through the exit tax therefore it is possible to prevent the transfer of intangible goods, like intellectual properties or patents, to low or zero tax jurisdictions with the aim of avoiding the tax payment on the economic value of the capital gains originating from their sale.

“Transfers of assets, including cash, between a parent company and its subsidiaries fall outside the scope of the envisaged rule on exit taxation”²¹⁹, that, as opposed,

²¹⁶ 2016/1164/EU, cit..

²¹⁷ *Ivi*, Article 9.

²¹⁸ Rosebuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 115.

²¹⁹ 2016/1164/EU, cit..

concerns: the transfer of assets from the head office to a permanent establishment in another Member State or in a third country; the transfer of assets from a permanent establishment in a Member State to the head office or another permanent establishment in another Member State or in a third country; the transfer of the tax residence to another Member State or to a third country “*except for those assets which remain effectively connected with a permanent establishment in the first Member State*”²²⁰; and the transfer of the business carried on by a permanent establishment to another Member State or to a third country. In these circumstances the exit tax applies in so far as the Member State of the head office or of the permanent establishment “*no longer has the right to tax the transferred assets due to the transfer*”²²¹.

The tax base for the calculation of the exit taxation is constituted by an “*amount equal to the market value of the transferred assets, at the time of exit of the assets, less their value for tax purposes*”²²². So the Directive renounces to consider the market value at “arm’s length”, in favour of the fair value, that is given by the market value less the fiscal value.

- The need of tackling efficiently the aggressive tax planning, so to say the adoption of abusive and harmful tax practices, requires the introduction in the legal systems of the Member States of general anti abuse rules (GAARs).

Indeed, general anti abuse rules are fundamental for the Member States in order for them to be able to face abusive tax practices that have not yet been dealt with through specifically targeted provisions. Thence, GAARs have a function of integration of

²²⁰ *Ibid.*

²²¹ *Ibid.*

²²² *Ibid.*

the specific anti-tax avoidance provisions, scilicet of filling in gaps of the current national legislation.

Besides, the Directive recommends, for the purpose of ensuring a right functioning of the GAARs, that they are applied in a uniform manner in domestic situations, within the EU and in relation with third countries, “*so that their scope and results of application in domestic and cross-border situations do not differ*”²²³.

The Article 6 indicates, for the calculation of the corporate tax liability, not to take into consideration the presence of arrangements, mainly aimed to gain a tax advantage, that are not genuine. Then goes on saying that arrangements are non-genuine “*to the extent that they are not put into place for valid commercial reasons which reflect economic reality*”²²⁴.

This qualification of the harmful practices not only as artificial but as non-genuine arrangements, marks the acknowledgement, from the European institutions, of the presence of a subjective element in the aggressive tax planning; of a fraudulent attitude towards the law, typical of the abuse of right. Moreover, in the Directive there is another element that is expression of this changed vision of the tax avoidance arrangements, and is the Whereas (11), in which is claimed that “*Member States should not be prevented from applying penalties where the GAAR is applicable*”²²⁵. In fact, as already outlined above in 5.1, the possibility of applying sanctions is subordinated to the recognition of the presence of a psychological element, of a harmful will. Otherwise, only the rectification of the calculation of the tax base could be imposed. Which in practice means the

²²³ *Ibid.*

²²⁴ *Ibid.*

²²⁵ *Ivi*, Whereas (11).

application of the provision as if the artificial arrangement had not been created, without the possibility of issuing any kind of sanction.

Scheme about the principle of the protection of the internal market and of the tax base²²⁶:

TRANSNATIONAL COMMON PRINCIPLE	Protection of the internal market and of the national tax base. UE/BEPS
MIDDLE LEVEL PRINCIPLE	The enterprise has to pay taxes in the place where the profits and the added value are created. Money laundering, corruption, crime organizations, financing of terrorism
EVALUATIVE STANDARD	<ul style="list-style-type: none"> • Interest limitation rule • Controlled foreign companies(CFC) • Tax arbitrage • Exit tax (only EU) • Avoid tax avoidance through permanent establishment • Grant the consistency between transfer prices and the value created

²²⁶ Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., p. 135.

5.4 Harmful tax competition

The objective of hindering the harmful tax competition is the fourth and last principle of the good tax governance. It reunites in itself the necessity of fighting the tax avoidance and the tax evasion as well as the money laundering, the corruption and the financing of terrorism; and it also represents a concretization of the other principles of corporate social responsibility, of transparency and of protection of the internal market and of the tax base. The concept of harmful tax competition, whose first version dates back to the Code of Conduct for business taxation of the Monti package of the 1997, basically consists in the activity of Member States that arrange juridical or administrative structures whose target is not to offer an incentive or to carry out a promotional function of economical nature, but rather to offer fiscal immunity. This way, they unfairly try to attract foreign profits and assets in exchange for fiscal immunity or opacity. Another case of harmful tax competition occurs when the Member State favours resident persons by giving them fiscal benefits to invest in and/or access to foreign markets. Incentives that instead are denied to non-residents. Therefore, not only attracting capitals and activities from abroad is an harmful practice, but also giving to resident tax payers advantages that, without the intervention of the State, they would not have the possibility to access to²²⁷.

The tax competition is qualifiable as harmful when it is liable to cause a damage to the fiscal interest of the other States. It harms the right of other States to levy and collect taxes, violating international fairness principles and stealing economic capacity to their tax base.

The harmful tax competition is made of tax avoidance and evasion made by the State. There is tax avoidance when the State provides for a preferential tax regime for non-resident taxpayers not available for residents, or when it offers juridical instruments that

²²⁷ Rosebuj T., *I principi e la tax governance nell' Unione Europea*, cit., pp. 123-124.

grant fiscal benefits even when an economic activity lacks, or also when mechanism are arranged that exempt residents from the tax payment when they access to foreign markets. As opposed, there is tax evasion when the State institutionally hides profits and capitals coming from abroad thanks to its opacity in the fiscal system and in the information regarding the beneficial owner²²⁸.

The unfair tax advantage, beyond jeopardizing the fiscal interest of the other States, is also a threat to the fair commercial competition. Indeed, it violates the fundamental prerequisite of the fair commercial competition, that is the equality of conditions. Thence, the State aid is a prejudice for both the tax and commercial competition, and twists the economic exchanges.

With specific reference to the European Union, as an element of the good tax governance, the principle of fair tax competition forbids the usage, within the Single Market, of any kind of State aid leading to the minimization of the tax burden. For instance, several times since 2003, the EU has expressed its concern about tax rulings illegitimately used as State aid instruments, establishing *ad hoc* advantages for specific companies, manipulating the determination and evaluation of intra-group transactions through the transfer prices. Transfer pricing rules, in fact, provide for the application of the arm's length principle: that means that the transfer price cannot be arranged through administrative agreements, like tax rulings, but rather, in determining its amount for fiscal purposes, it has to comply with the market value. In other words, it has to be equal to what would have been established if the companies considered were independent. Indeed, tax rulings are often used as means to manipulate the movement of profits within the parent company and its subsidiaries,

²²⁸ *Ibid.*

succeeding in reducing significantly the tax burden, or in shifting its payment to other jurisdictions.

The European position regarding State aids is based on three main statements: first, the State aid is prohibited when it offers a more favourable fiscal treatment for only a part of the taxpayers, placing them in a privileged position; second, the tax system is not acceptable when it proposes a method for determining the tax base of a group that is not a reliable approximation of the market based outcome, and concede illegitimate benefits like the minimization of the tax base and of the tax burden; and third, tax rulings grant the legal certainty until they do not establish benefits ad hoc for specific subjects.

Following to the reconnaissance of a case of State aid, the consequence is the duty of the State conceding the illegitimate aid or the right of the damaged third States, of recovering the amount of money establishing an unfair competition, with a retroactivity of ten years²²⁹.

Another fiscal instrument potentially dangerous for a fair tax competition is the patent box. A patent box is an instrument that offers a preferential tax rate for income deriving from the use of intellectual properties. It establishes a link between the expenses for the creation of the intellectual property, and the income deriving from its utilization. And, differently from the other R&D incentives, that are provided when the expenses are incurred, patent boxes, reduce taxes when, and if, income is earned²³⁰.

The intangible goods considered for the patent box are patents, copyrights, software, and all the other goods equivalent to patents, excluded brands. And for the calculation of the fiscal benefit, the profit of the intellectual property is given by the royalties and capital gains arising from the sale of the intangibles and from the sale of products or processes

²²⁹ *Ivi*, 127-128.

²³⁰ Graetz M.J. & Doud R., *Technological Innovation, International Competition, and the Challenges of International Income Taxation*, Columbia Law Review, 113(2), 2013, pp. 347-445.

directly linked to the intangible good; whereas, the expenses are the ones that contribute to increase the profit of the IP and are made either by the enterprise itself or through the purchase from other enterprises.

The European Union has always shown doubts regarding patent boxes, because of their possible use as a mean of harmful tax competition. The main concern is about the possibility of exploitation of patent boxes for operation lacking a real economic substance: for instance, patent boxes can be used to encourage income shifting by attracting income away from the country where the underlying R&D took place. In order to put a remedy to this, the EU provided for the emendation and actualization of the Code of Conduct for Business Taxation and adopted the solution proposed by the BEPS Project in the Action 5: the so called the nexus approach. Under the nexus approach, it is established the maximum amount of IP profit that can receive the tax benefit, so that countries are only permitted to provide benefits under patent boxes if those benefits are proportionate to the amount of R&D undertaken by the taxpayer receiving benefits or in the country providing benefits²³¹. Therefore, it is also confirmed the necessary presence of a substantial economic activity to grant the benefit of the patent box²³².

Scheme about the principle of harmful tax competition²³³:

COMMON PRINCIPLE	Harmful tax competition
MIDDLE LEVEL PRINCIPLE	<ul style="list-style-type: none"> • Actualization of the Code of Conduct for Business Taxation

²³¹ Faulhaber L.V., *The Long Reach of European Union Law: Patent Boxes and the Limits of International Cooperation*, Georgetown University Law Center, 2015.

²³² Rosembuj T., *I principi e la tax governance nell' Unione Europea*, cit., pp. 129-131.

²³³ *Ivi*, p. 136.

	<ul style="list-style-type: none">• Preferential tax regimes
EVALUATIVE STANDARD	<ul style="list-style-type: none">• State aid• Patent box• Tax rulings

Conclusion

In conclusion, the results of the argumentations made throughout this work, in spite of their apparently purely theoretic nature, are, as demonstrated, highly relevant in practice.

First of all, in chapter I, it has been described the importance of adopting a principle based regulation. After having analysed what the principles are, how they are created, and what is their relation with the spirit of the community and with moral values, it has been argued their importance in the interpretation and application of the laws, especially nowadays with a significant increase in the complexities of the facts.

The all-or-nothing way of application of the laws has been recognized as inappropriate to answer to the incredible variety of circumstances of the reality, and only the auxiliary intervention of principles can help finding the right solution and lead to a real justice.

All these factors make clear as a strict application of a purely positivist vision of the law, based on the idea of the rule of law, is not sustainable any more. And this has also brought to the development of the so called governance.

It has been explained as the governance, that is a system based not on authority, but rather on coordination and cooperation, is the reaction and the natural outcome deriving from the deficiencies of the hard law. It is characterized by the intervention of multiple actors, at different level, and, above all, by the informality of the processes and by the utilization of common principles and of instruments of soft law.

Term soft law that indicates a complex of soft regulation, based of flexible regulatory instruments, whose main characteristics are the non-formal procedure for their adoption, and their non-binding nature. These two features make the soft law the perfect tool to

manage matters that require quick procedures for adopting and emending rules and openness to possible new participants on a purely voluntary basis.

This is exactly what noticeably happens in the European Union (chapter II), where the governance and the use of the soft law have definitely taken place in many different matters, in particular in the tax field. The general reluctance of the Member States to delegate fiscal competences to the European Union and the progressive erosion of the national tax bases with the consequent loss of revenues, have pushed the Member States and the EU itself to develop a system of hybrid and multilevel governance, based on coordination rather than harmonization, able to tackle efficiently the modern issues of international taxation and, above all, thanks to the implementation of the rules on a voluntary basis, to overcome the paralysis often produced by the unanimity rule that the Fundamental Treaties of the European Union provide for the adoption of fiscal provisions. On these basis, in the last decades, the European Union progressively developed the principles of good tax governance, through which it indicates the principles that has to guide the tax system of each Member State and the EU as a whole. Good tax governance principles that specifically are: the corporate social responsibility, the transparency, the protection of the internal market and of the tax base, and the harmful tax competition.

After having verified the widespread use of soft law and having explained the reasons behind this evolution in the regulatory methods, it is not possible to evade an issue that is becoming increasingly pressing, proportionally to the growth in the use of the soft law: the question of democracy. As already briefly outlined, when the consequences deriving from the decision of not complying with certain soft rules become so heavy and detrimental for a State or for some other subject like enterprises or banks, the soft law, from being a non-binding instrument, substantially turns into a binding one, and the subjects addressed by

the rules cannot actually be considered any more free to adhere to them or not. This situation, of course, poses an issue of lack of democracy: indeed, the absence of a specific mandate from the electors to the body issuing the soft law and the absence of a legislation formally regulating the procedure for adopting the acts, together with the fact that the soft law does not provide a full judicial protection, should prevent that same acts to exert a binding effect. The same demand for democracy arises when a certain field is almost entirely regulated solely by the soft law. For instance, in the European Union, the tax matter is one of these cases: the unanimity rule is now constantly *de facto* bypassed through recommendations, communications and other acts of soft law. And this means that the hard legislation (the European Treaties in this particular case), adopted following to rigid and democratic procedures, is totally and continuously ignored, even if formally without violating it, by using the soft law as its surrogate.

The European Parliament itself has expressed its concerns about this situation in a Resolution²³⁴ in which it claims, among the many implications in the use of soft law, that the EU Institutions should only act in accordance with the principle of legality, that is to say, only where a legal basis confers them competences and within the limits of their powers, always remembering that there is a European Court to ensure that they do so. In addition to that, it raises its worries for the fact that the “*Parliament, as the only democratically elected Community institution, is not currently consulted about the use of so-called soft-law instruments*”²³⁵ and therefore it also “*calls on the Commission to develop, in cooperation with Parliament, a modus operandi that guarantees the participation of the democratically elected bodies*”²³⁶.

²³⁴ 2007/2028(INI), *European Parliament resolution of 4 September 2007 on institutional and legal implications of the use of "soft law" instruments.*

²³⁵ *Ivi*, n. 14.

²³⁶ *Ivi*, n. 16.

From this non democratic situation there is not an easy way out. In fact, if on the one hand the demand for democracy is totally well-founded and cannot be ignored, on the other hand, it has been explained as the necessity to overcome the formalities and sometimes the paralysis of the European legislative procedures, especially in the tax field, is crucial in order to be able to give an answer to the continuously changing situations of nowadays and to the threats of the harmful tax practices; and thence, a return to a rigid and purely positivist approach to the law, based on the idea of the rule of law, is not absolutely advisable. Clearly, compromises will have to be found, and probably the hypothesis of eliminating the unanimity rule, together with a major openness of the Member States towards the delegation of relevant fiscal competences to the EU Institutions, or at least an involvement of the European Parliament in the procedures for the adoption of the soft law instruments, would definitely be relevant steps forward in the direction of a compromise, that anyway, will be anything but easy to be found.

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