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Tax Controversy

Introduction

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COVID-19

Given the ongoing context of the pandemic, governments have adopted unprecedented measures, along similar lines, to protect the health of individuals and to sustain their economies, whilst supporting families and companies to enable them to resist the economic slowdown. Strict quarantine requirements were applied everywhere: closed borders, travel bans, shuttered businesses and restrictions on the right to go out. Teleworking, whenever possible, became the norm almost globally, with few exceptions. Courts were closed or not, depending on the countries in question, but many activities including hearings started being held by videoconference, and deadlines and terms related to pending or new cases were suspended – at least for a while. Indeed, as the UK contributor suggests in the **UK Trends & Developments** chapter, it may be that judges and parties become more comfortable with holding procedural hearings by conference or video call even in the medium-to-long term, after COVID-19 restrictions are lifted.

During the last year, governments have been supporting individuals and companies in need with measures that postpone tax payments or embrace flexible approaches towards compliance with specific obligations. Public spending has increased substantially, and it is expected that the pandemic crisis will leave the world deeply in debt. The situation is naturally different in each country, but some fear new taxes will be created and at the same time predict that the tax authorities will be inclined to be stricter and/or carry out more extensive audits (USA, Portugal, Mexico, etc). The **USA Trends & Developments** chapter not only mentions the way in which the COVID-19 pandemic continues to change the approach to tax controversies but also provides

some hints about the possible policy directions of a new White House.

More than ever, the management and control of tax risks is a primary goal for both tax authorities and taxpayers. For the former, it is disastrous if the State is unable to collect the expected level of revenue. For the latter, tax is a significant cost for business and an incorrect estimate can jeopardise a company's level of profitability and damage its reputation, not to mention cause egregious disadvantages and losses. However, it is now almost certain that, in the short term, debt and public expenses will increase while tax collection levels will drop due to the economic contraction.

It might be debatable whether, as some have argued, taxes are a prime mover of history. One cannot ignore facts, however. We have the recent memory of the American experience after the 2008 crisis when both tax authorities and MNEs were in need of revenue and neither was prepared to compromise easily. Currently, it seems that the IRS, as well as several other tax authorities, is focusing more of its attention on international tax issues and, more specifically, transfer pricing. It is interesting that, due to a lack of resources, there is a move towards concentrating activity under a new strategy: the “campaign”, whereby the IRS's Large Business and International Division selects a tax issue for audit, rather than auditing every potential issue on a taxpayer's return.

Anticipated Increase in Tax Litigation

Inevitably, no one can anticipate and eliminate entirely the potential adverse situations that lead to disputes. Although disagreements may emerge suddenly and in relation to all type of taxes, the majority of chapters in this Guide refer

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to the many international, complex and controversial substantive tax matters around the BEPS Recommendations and the legislation created afterwards, the MLI, digital taxation and the use of the general anti-abuse rule (GAAR) to challenge cross-border transactions, although many of them cannot ascertain whether these have so far contributed to an increase in the level of tax controversies. But there are already many authors anticipating more litigation. Some, like the **Netherlands Law & Practice** chapter, emphasise that since jurisdictions may interpret the BEPS rules in their own manner, this will attract more litigation. The same expectation exists with respect to the impact of the EU Mandatory Disclosure Directive (DAC 6) and many other jurisdictions within the European Union mentioned the same scenario. On the other hand, in the UK chapter, it is stressed that even if the EU measures are less relevant in the UK than previously, Brexit will result in significant amounts of tax legislation, so there is significant potential for tax controversy in the coming years.

The amount of new legislation everywhere, and the appearance of new and open concepts applied worldwide in a context of states struggling for financial resources, creates an expectation of increased litigation, as several other chapters suggest. Moreover, new international instruments such as DAC 6 and the MLI are expected to have significant impact on how anti-abuse rules will be applied, which will probably increase litigation.

The tax authorities of each jurisdiction might have different perspectives and approaches on how to combat non-compliance with tax obligations or tax avoidance. Nevertheless, they are all undoubtedly better equipped and prepared, with substantial information at their disposal about taxpayers, as well as their own activity, and they are much more integrated internation-

ally, as several chapters, including the **USA Law & Practice** one, mention.

Audit Strategy and the Road Ahead

Perusing the chapters in this Guide, it is noticeable that taxpayers, even multinational enterprises (MNEs) and high net worth individuals (HNWIs), are often caught in the crossfire created by the competition between states for capital and investment, and suffer from a changing and uncertain compliance landscape. It is therefore extremely valuable to know how to anticipate, prepare for and manage possible audits or to verify whether it is possible to eliminate or mitigate tax risks, either before or during a specific controversy.

This Guide presents an excellent overview of the main aspects of the tax controversies that are common and distinct in 27 very different jurisdictions (from Afghanistan to Rwanda and Macau but also covering several EU member states, the UK, the USA and Japan), providing a very interesting global analysis of trends:

- the origin and causes of tax controversies;
- the continuous efforts to combat tax avoidance and evasion;
- the means to mitigate and manage tax risks and to stay up to date with the best ways to settle cases; and
- the strategies to employ in the context of administrative or judicial litigation.

The reader will also be able to gather comparative information on all the phases of tax litigation in each jurisdiction, either in domestic or cross-border disputes, and will be able to garner an idea of costs and statistics in the area of tax litigation, including the number of cases and the likelihood of a successful outcome for either the tax authorities or taxpayers.

International Tax Authority Co-operation

It is clear from all the chapters that tax authorities are collecting more and more information concerning taxpayers, and their businesses and cross-border activities (either through exchanges of information and mutual assistance or through the country-by-country (CbC) reports, the common reporting standard (CRS) or other mechanisms or groups (eg, the Joint International Taskforce on Shared Intelligence and Collaboration)). Soon the reporting obligations foreseen in DAC 6 will also be automatically exchanged in the EU. Whether one is in Italy, the UK, Japan, Brazil or the USA, the tax authorities now know more than in previous years. Given the specific circumstances, culture and approaches in each jurisdiction, there is no unanimity as to whether this has been leading, or will lead, to an increase in tax controversies but several assertions and hints suggest so, at least in some countries.

Litigation and Tax Authority Approaches

According to the chapters in this Guide, it seems that some tax authorities are investing in minimising tax disputes, either helping taxpayers effectively via direct contact, tax rulings or through the use of alternative dispute resolution mechanisms. It seems that this open approach pays off, considering that when litigation occurs, the tax authorities claim a higher success rate before the tax tribunals or higher courts, as emphasised by the **New Zealand** and **Switzerland Law & Practice** chapters.

In countries where the tax authorities seem more reluctant to invest in assisting taxpayers dealing with complex legislation and ambiguous matters, additional tax assessments have grown significantly, which also gives rise to an increase in the number of controversies. Unsurprisingly, this reflects negatively on how investors evaluate the “tax element” when researching the different aspects of doing business in that specific jurisdiction. The case of Brazil seems to be an

example, although several changes and reforms in course may change this perspective, as the **Brazil Trends & Developments** chapter suggests. In these countries, taxpayers can prevail more often.

The tax legislation and the tax authorities’ approach in some other countries, meanwhile, seem to occupy a middle ground between the types of patterns described above. Statistics regarding the success of the tax authorities in litigation seem to be in line with this, for instance in Portugal and Spain.

Efficient alternative dispute resolution (ADR) mechanisms may also be very helpful in preventing/reducing disputes, or at least resolving them quickly, as the Portuguese domestic arbitration system shows. But the administrative attitude and the taxpayer culture still seem to be the crucial elements, ie, without a willingness on the part of both the authorities and taxpayers to work collaboratively, and with reasonable alacrity, ADR mechanisms may not be sufficient.

Criminal Tax Controversies

This Guide also illustrates the way tensions may be avoided as they arise and may evolve from tax audits up to the higher tribunals, either through administrative and civil discussions where anti-avoidance rules, including transfer pricing, still play an important role; or in the context of tax evasion or fraud – involving, for example, dishonest conduct and false accounting – when such matters will usually be treated as crimes, and where the proceedings and the investigations are conceptually separate and evolve independently. The Guide explains the differences, the possible interactions between tax assessments and tax infringements and the possibilities to reduce fines and/or to initiate and conclude settlements. In some countries we notice that there is an increased risk of criminal

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liability, not only for the taxpayers themselves but also for the so-called facilitators.

Litigation Strategy

At the same time, the reader is guided by each author through different geographies along the administrative and judicial routes, from the first to the final stages (that is, considering administrative hierarchical or judicial appeals), considering deadlines, intricate proceedings and rules and principles that reveal how disputes may be settled in the most appropriate manner.

Despite the existence of absolutely different procedural rules and ways to settle tax disputes, we observe several important common features that contribute to taxpayers' best interests, which are stressed by the majority of authors.

These include:

- the importance of being prepared before an audit has even started and of being assisted by a legal adviser from the first hour;
- the need to be fully conversant with all the relevant facts around the potential controversy and to evaluate the risks and associated contingencies in order to minimise them;
- supporting the facts and bolstering the substance of the case, disclosing documentation and engaging expert assistance, or any other necessary support;
- verifying if the dispute may be narrowed, either by settling or abandoning any of the issues, but making wise use of all procedural and material rights; and
- the importance of an awareness of previous case law, even in civil law jurisdictions where precedent does not have the same strength as in common law systems, an importance that increases with the need to know international jurisprudence from the ECJ or the ECHR and even being aware of comparative jurisprudence or doctrine.

Naturally, in-depth analysis of a case, its facts and the applicable rules of law are crucial to mastering tailor-made strategies for individual cases, as this Guide repeatedly emphasises. The reader will certainly understand that, in spite of globalisation and of similar concepts/substantive tax issues (such as transfer pricing matters, hybrid mismatches, recharacterisation issues or cross-border disputes after BEPS) or procedural rules and principles, the way disputes may best be settled in each country is still part of the expertise and art of practitioners in the respective jurisdictions.

International Issues

The different chapters also emphasise the use of domestic or international tools, such as the mutual agreement procedure, to solve cross-border disputes, indicating how they usually interact. Some of the chapters allude to the MLI, considering that it is already in force in several countries, and provide an idea of the crucial matters (eg, the **Netherlands Law & Practice** chapter).

It is also interesting to observe that GAAR and SAAR (specific anti-abuse rule) application in a treaty context have already been challenged in several court cases. However, the majority of chapters choose to stress the confidence in their compatibility that the tax authorities and states have repeatedly invoked (along with the OECD Model Tax Convention commentaries), suggesting that taxpayers should, if not must, adopt conservative approaches in exploiting DTT opportunities. The MLI also contributes to changing the situation, in particular considering the "saving clause" (Article 11).

The fight for income from international taxation ignites intense discussion, not only among taxpayers but also among different tax authorities and states. The appearance of so many new tools and weapons to combat tax avoid-

ance allows us to predict that tax disputes will increase, unless a great investment is made in assisting taxpayers on a daily basis and in creating ADR mechanisms. Ironically, it seems that at the same time that an avalanche of new measures have been created to combat taxpayers' abuses (BEPS, DAC 6, etc), states have felt the need to create quick arbitration mechanisms to settle tax disputes between themselves (eg, the MLI and the EU Arbitration Directive).

Conclusion

Authors from several jurisdictions predict, in the near future, stricter audits and additional tax assessments, and possibly even more taxes. After the COVID-19 crisis elapses, however, the authorities will have to consider the approach to "recovery" when states will want to preserve their business sectors considering the need for

a long-term economic growth. In any case, given the current circumstances, taxpayers should clearly be more proactive in their internal audits, analysis, and management of their tax risks.

Considering that every move takes time and that the state of the art in each jurisdiction is at a different stage of development, the present guide is an excellent tool for professionals – tax lawyers, barristers, and in-house lawyers, but also company CFOs and members of their departments, tax consultants, judges, or other professionals – to provide a compass in finding the right path when preparing and handling a tax audit or controversy; either to assist in managing a good settlement or, if this proves unworkable, conducting a successful dispute.

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Morais Leitão, Galvão Teles, Soares da Silva & Associados (Morais Leitão) is a leading full-service law firm in Portugal, with a solid background and decades of experience. Widely recognised, Morais Leitão is a reference in several branches and sectors of the law at the national and international level. The firm's reputation amongst both peers and clients stems from the excellence of the legal services provided. Morais Leitão's work is characterised by its unique technical expertise, combined with a distinc-

tive approach and cutting-edge solutions that often challenge some of the most conventional practices. With a team comprising over 250 lawyers at its clients' disposal, Morais Leitão is headquartered in Lisbon and has additional offices in Porto and Funchal. Due to its network of associations and alliances with local firms and the creation of the Morais Leitão Legal Circle in 2010, the firm can also offer support through offices in Angola (ALC Advogados) and Mozambique (HRA Advogados).

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Francisco de Sousa da Câmara is a senior partner at Morais Leitão who has headed the tax teams in Lisbon and Madeira for more than two decades. He specialises in complex tax litigation involving domestic and international tax issues, and focuses on handling files before all types of courts. He is

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