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Abstract: This article argues that tax is a hybrid of civil and common law, public and private law, and is cross-disciplinary. It observes that tax law has become an all-purpose tool for legislators. It seeks to demonstrate how the US, a common law jurisdiction, has turned to civil law models for taxation while civil law jurisdictions and the European Union have sought common law models to combat tax avoidance. The ubiquity of tax and its public law influence on private law transactions, its cross disciplinary nature, and its deployment as a legislative tool to manage the economy make it a candidate for reform targeting cross-border uniformity and systemic convergence—a motion that has begun and should continue to reach full uniformity.

Keywords: *taxation; tax planning; civil law; common law; public law; private law; legal convergence; cross-disciplinary*

I. Introduction

Statutes and codes dominate the income tax. As the late Professor Frans Vanistendael observed: "it is inevitable that the legislator cannot foresee all situations in a rapidly

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changing world"[1] so that courts and administrative agencies often are left to determine application of the income tax to prevent exploitation of limited statutory language to capture unintended tax benefits. Income tax is public law and yet shapes many, perhaps most, transactions in the private law sphere. Lawyers, accountants, financial planners and others interpret and advise on income tax matters without significant differentiation in their roles or licensing requirements. Legislatures utilise the income tax to deliver economic incentives and in so doing make the tax laws complex as the taxing agency must administer nontax governmental programmes. Tax is indeed a hybrid of civil and common law, public and private law, and is cross-disciplinary. And tax law has become an all-purpose tool for legislators.

In the US, tax law relies on an extensive statutory base in an historically common law country. Following adoption of the income tax amendment to the US Constitution,[2] the income tax developed through judicial decision-making that embellished and limited simple, general statutes. The legislature tended to follow the courts with legislation codifying and sometimes reversing judicially determined outcomes. Over the years, however, US courts have become increasingly reluctant to fulfil that common law role and supply substance for income tax statutes. The courts cede that role to the legislature. Responding to courts' restraint and expressing legislative interest in controlling the development of tax law and using it to subsidise politically advantageous projects for their constituents and donors, statutes have become ever more complex and precise. Concomitantly, courts have become ever more reserved in broad interpretation of the statutes so that ambiguity in application generally has worked in the taxpayer's favour except in the most egregious tax avoidance contexts. Tax law in the US has become predominantly statutory and civil law-like.

In the European taxation world, on the other hand, civil law dominance and predictability of tax outcomes have retreated. Civil law jurisdictions have become common law-like in relying on the courts and taxing agencies to limit and define taxation rules. Constitutional courts have assumed increasingly important roles in the application of tax statutes and have supplemented their more traditional role in determining whether a statute meets general constitutional requirements before it becomes law.[3] Constitutional courts have given the legislature specific instructions on modifying statutes to render them constitutional.

The uncompromising precision and certainty in application of tax rules that taxpayers anticipate under civil law has yielded to ambiguation requiring intervention of the courts. Several jurisdictions have adopted general anti-avoidance rules (GAARs)[4] that,

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1 Frans Vanistendael, "Legal Framework for Taxation" in Victor T Thuronyi (ed), *Tax Law Design and Drafting* (International Monetary Fund, 1996), Volume 1, 15.

2 US Const Amend XVI (1913), the United States could impose a direct tax on incomes without apportionment among the states. Before enactment, the apportionment clause prohibited unapportioned taxes. US Const art.I, § 9.

3 Eg, see Conseil constitutionnel in France.

4 Eg, see Germany: Abgabeordnung (AO) §42(2), available at https://www.gesetze-im-internet.de/ao_1977/__42.html accessed 12 August 2023, recasts the tax outcome if it would not coincide with the intention of the legislation. Similarly in Sweden, Lag (1995:575) mot skatteflykt, as amended by Lag (2011: 1372), available at https://lagen.nu/1995:575 accessed 19 August 2023, allows tax agency to disregard transactions the primary purpose of which are to capture a tax benefit. See generally John Prebble KC, "General Anti-Avoidance Rules: Enactments from the World" (Victoria University of Wellington Legal Research Paper No. 170/2017, WU International Taxation Research Paper Series No. 2018-01, 2017), available at https://ssrn.com/abstract=3088222 accessed 12 August 2023.

when applied by the tax collector, leave the courts as the ultimate arbiter of the tax outcomes, sometimes seemingly contrary to statutory language.[5] Determination of facts and legislative intent drive the application of GAARs since, unlike other civil law legislation, GAARs are not self-executing. In addition, EU institutions have assumed a non-statutory role in the application of tax law. The European Commission adopted a broad anti-tax avoidance directive (ATAD),[6] and the Court of Justice of the European Union (CJEU) has assumed an outsized role in shaping limitations on taxing legislation throughout the EU where the taxation issue may have implications across national borders and where national governments seek to deploy the tax system to provide economic incentives for investment.

This article focuses on the ubiquity and importance of tax law in the US and Europe. The article observes the transition of tax law in the US into an increasingly civil law system and in Europe, with emphasis on Germany, the growing role of the courts in shaping tax law as is consistent with common law legal systems. Section II discusses the fundamental importance of tax law, a public law discipline, in decision-making in the private sphere, highlights the overall reach of tax in modern economies, and emphasises the economic domination of tax in practice. Section III illustrates the judicial role in developing the tax law in the US under broad and general statutory drafting and the change in legislative drafting style to render tax rules more complex and specific. Introduction of detailed statutes has limited the courts' role in further development of tax law as the US trends towards a civil law in the presence of statutes and codes. Section IV observes the constitutional court in Germany transforming itself into a common law court as it shapes interpretation of taxation legislation and directs the legislature to revise legislation to meet its interpretations. Section V reviews some decisions of the European Court of Justice acting as a common law type court in limiting legislative flexibility throughout the EU with respect to taxation to comply with the EU's governing treaties.[7]

Section VI considers ambiguation of tax law and the extra-statutory role of the courts play in combatting tax avoidance. General interpretive authority under GAARs in civil law jurisdictions parallels the development of non-statutory interpretive doctrines in early US tax history. The ATAD encourages the influx of GAARs into the civil law, even though GAARs would seem a common law tool. Section VII concludes that the borrowing and converging of tax law has been accompanied by the merging of common and civil law in the tax law world, so that tax has become a hybrid of the two discrete systems. Hybridisation is critical to the success of the Base Erosion and Profit Shifting (BEPS) projects[8] since without a common tax base and common rules of application,

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5 Eg, see the Cum-Ex cases, discussed below in Section III.

6 Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market, available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2016.193.01.0001.01.ENG&toc=OJ:L:2016:193:TOC&print=true accessed 24 August 2023.

7 Consolidated Versions of the Treaty on European Union and the Treaty on the Functioning of the European Union (2016/C 202/01), available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex-%3A12016ME%2FTXT accessed 28 August 2023.

8 The Organisation for International Cooperation and Development (OECD), "BEPS: Inclusive Framework on Base Erosion and Profit Shifting", available at https://www.oecd.org/tax/beps/ accessed 27 August 2023.

BEPS cannot succeed. Too many ambiguities and uncertainties will plague the computation of a minimum tax, for example, where base differences are prominent.

II. Tax Ubiquity: Public Law Driving Private Law Transactions and Fuelling a Tax Planning Industry

In any public law/private law taxonomy, taxation is public law because it defines and regulates interactions between governments and taxpayers.[9] Yet, taxation drives the structures of private commercial and personal transactions and sometimes motivates taxpayers to alter even the economic outcome of the transaction to capture an available tax advantage.[10]

A. Multi-level tax planning and revenue loss

Acquisition, commencement, and choice of legal form of a business, as well as the structural details of transactions frequently depend upon tax analysis. Tax outcomes do not necessarily correspond to economic results. Often tax and economics differ significantly depending on transactional forms. Structural adjustments alter tax consequences even in the presence of substantially identical, non-tax, economic outcomes independent of those transactional choices. Non-statutory interpretive doctrines such as "substance over form"[11] enable tax collectors occasionally to disregard artificial transactional structures designed solely to capture a tax advantage but, in most instances, taxpayers can identify an adequate business purpose to support a transactional structure and prevent the tax collector from disregarding a taxpayer's structural choice. Where valuable tax differences exist for different structures, but the differing structures produce substantially identical economic outcomes, the tax law reveals its complexities and inefficiencies.

A tax system that provides opportunities for capturing tax advantages without materially altering economic outcomes fuels the outsized tax planning industry. That industry consumes extensive intellectual and financial resources to the detriment of national economies.[12] In addition to the deadweight loss to the national economy from reduction of tax burdens for affluent taxpayers through sophisticated tax planning, legislative observation of such planning encourages legislatures to shift tax burdens to those least able to develop tax avoidance strategies. During the last half century, there has been a readily observable shift of tax burdens from capital to labour because labour has found limited opportunities to exploit tax planning to diminish tax obligations and is a relatively easy tax collection target through withholding on wage income and value added taxes on consumption.[13]

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9 Jean Baron MJ van Houtten and Charles E McLure, "Tax Law" *Britannica* (updated July 2023), available at https://www.britannica.com/money/topic/tax-law accessed 16 August 2023.

10 During the latter half of the 20th century, taxpayers engaged in many economically unsound and losing investment schemes to seize available tax benefits and diminish their obligations to pay taxes. Henry Ordower, "The Culture of Tax Avoidance" (2010) 55:1 *Saint Louis University Law Journal* 47.

11 *Gregory v Helvering* 293 US 465, 469–470 (1935).

12 Klaus-Dieter Drüen, "Unternehmerfreiheit und Steuerumgehung" (2008) *Entrepreneurial Freedom and Tax Avoidance* (author's translation), 85:2 *Steuer und Wirtschaft – StuW* 158.

13 Henry Ordower, "Capital, an Elusive Tax Object and Impediment to Sustainable Taxation" (2020) 23:1 *Florida Tax Review* 625, 641–646.

In the US non-business world, some, primarily capital, tax-based choices yield more favourable outcomes than alternatives. For example, a grandparent about to make a large gift to a grandchild may elect to encumber appreciated property and make a cash gift of the borrowed funds rather than making a gift of the appreciated property itself, even if the grandparent might prefer the property gift. Tax drives that choice because holding the property until the grandparent's death will eliminate the taxable gain on the appreciation embedded in the property.[14] Similarly, spouses negotiating the terms of their separation and divorce must evaluate the most tax efficient way to uncouple their interests,[15] and an injured individual recovering compensation from a tortfeasor, for reasons of tax efficiency, may choose a structured settlement with periodic payments at a non-taxable but low rate of return rather than a lump sum amount over which the injured party might control the investment and find a greater return but the investment return will be taxable.[16]

B. Tax and religion

Despite separation of church and state under the US Constitution,[17] religious law also impacts tax law. The US indirectly funds churches by allowing a deduction from taxpayers' otherwise taxable incomes for the contributions to churches, thereby subsidising the church contribution to the extent of the donor's tax reduction from the deduction,[18] not taxing gain on appreciated property contributed to a church, excluding from gross income the value of housing provided rent free to parsons (and similar individuals),[19] and, historically, favouring married individuals in permitting them to split income for tax purposes even if the income is earned by only one spouse.[20]

C. Deployment of taxation for non-tax policy support

Tax is ubiquitous and varied. Whether monarchs require support for wars, churches need resources to build and maintain facilities to disseminate their religious views, or modern governments pay for services the citizenry expects them to provide, taxation is essential to provide the funds or services. Tax appears in the form of big general taxes like church tithes,[21] income, property, and value added taxes, or obligatory government service or little, targeted impositions like carbon, alcohol, tobacco, or even window taxes.

Taxation also has become a primary tool to advance governmental policies. The US delivers many, perhaps most, subsidies through the tax system rather than by direct payments.[22] Many tax-based subsidies result in deadweight loss to the economy, as they often

14 Section 1014 of the Internal Revenue Code of 1986, as amended, 26 United States Code, referred to throughout as IRC § (followed by a section number).
15 IRC §§1041 (no income or gain on transfer of property), 71 (alimony included in income).
16 IRC §104(a)(2) parenthetical (excluding income from personal injury awards, even the imputed investment return on a settlement requiring periodic payments to the injured party).
17 US Const Amend I.
18 IRC §170.
19 IRC §107.
20 IRC §1. Marriage has its origins in religious law.
21 Joshua Cutler, "A Hebrew Republic of Taxation? Henry George's Single Tax, Hebraic Law, and Unearned Income" (2021) 57 *Idaho Law Review* 227.
22 Tax-based subsidies appear in the annual Tax Expenditures list. US Department of the Treasury, Office of Tax Analysis, "Tax Expenditures" (June 2021), available at https://home.treasury.gov/system/files/131/Tax-Expenditures-FY2022.pdf accessed 12 August 2023.

cost more than a direct targeted subsidy would, are inefficient allowing an excess subsidy for high income taxpayers because they are tax affected through the marginal rate brackets,[23] and some tax subsidies fail to advance the targeted objective.[24]

D. Taxation and avoidance

Accompanying the omnipresence of taxes is the omnipresence of tax avoidance or evasion and the resources expended to prevent tax avoidance or punish tax evasion. Permanently building over windows to avoid window taxes, dodging military conscription to avoid mandatory governmental service, planning to minimise income or estate taxes, carousel fraud to evade value-added taxes, and complex investment schemes to duplicate tax refunds or rebates like the recent "cum-ex" trading structures that have proven extremely costly to Germany, Denmark and other European jurisdictions are some ways in which taxpayers have sought to avoid the governmentally imposed mandatory impositions. The avoidance and evasion methods have pitted the tax collector against an often better resourced private interest.

Historically, national governments negotiated and designed bilateral tax treaties to prevent the double taxation of income. Competent authority proceedings sought to resolve inter-jurisdictional taxation disputes where tax definitions or rules in one jurisdiction differed from those in a treaty partner's jurisdiction. Taxation discontinuities might burden commerce by resulting in taxation of the same income or property in more than one jurisdiction or may facilitate the failure to tax income in any jurisdiction.[25]

E. The need for uniformity in taxation

International commerce has expanded, especially in conjunction with technological development and delivery of goods and services electronically, and international interest in coordinating taxation structures across national borders has increased materially. With growing electronic commerce, tax must adjust to meet the challenge of locational irrelevance in production and delivery of goods and services. Complex commercial structures and growing electronic commerce with its locational irrelevance have caused the international tax community to focus less on the historical model of bilateral treaties and more on multilateral instruments for development of uniform definitions and rules across jurisdictions. Multilateral instruments support international commerce and limit tax competition among jurisdictions.

Distinctions in definitions and rules across borders facilitate tax competition among jurisdictions and opportunities for taxpayers to arbitrage those interjurisdictional tax differences to reduce their individual taxpaying responsibilities. The Organisation for

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23 Eg, see IRC §103 subsidizes the interest expense of state and local governments on their borrowings by excluding the interest that such governmental units pay on their borrowed funds from the taxable recipient's gross income. A state must price its debt instruments targeting a specific rate bracket that is not the maximum so that the after-tax interest is equal to a fully taxable debt for the targeted purchasers. If a purchaser is otherwise taxable at the maximum rate, buying the tax-exempt debt yields a higher after tax rate for that purchaser resulting in deadweight loss.

24 Opportunity zones, eg, IRC §1400Z.

25 Edward D Kleinbard, "Stateless Income" (2011) 11:9 *Florida Tax Review* 699.

International Cooperation and Development (OECD) has been a leader in developing international agreements on taxation principles. The OECD captured the signatures of 138 countries to pillar II of its recent BEPS initiative. Pillar II, the global anti-base erosion project, known as GloBE, would have all countries adopt a 15 percent minimum tax to limit tax competition and tax arbitrage.[26] Implementation of pillar II is proving elusive, however, and a uniform tax base and taxing rules across jurisdictions is critical to its implementation.

Nations long have borrowed tax concepts from other nations. Some of the borrowing was by design. For example, experts from Europe and the US assisted the formerly Soviet influenced or controlled states to develop operating tax systems after 1990 where a tax system had been unnecessary under their communist, centrally planned economic systems.[27] Borrowing causes tax rules and procedures to converge even where the tax systems differed considerably at their outset. Convergence of taxation rules and procedures and uniformity of taxation definitions becomes ever more critical to facilitate international commerce, accommodate international electronic transactions and confront borderless electronic cryptocurrencies and national parallel currencies.

Cryptocurrencies are especially challenging. They operate without the need for a central banking system and free from the constraint of individuals in control. Popular cryptocurrencies are autonomous with computer programmes managing transfers. While great strides have been made to identify use of cryptocurrencies for money laundering and governmental authorities have even seized cryptocurrency in some ransom instances, cryptocurrencies remain opaque with respect to tax reporting and evasion despite national efforts to require more extensive reporting primarily because no individual or entity manages the currency.[28] Uniform cross-border taxing rules are essential to successful control of the cryptocurrency world and collection of taxes from its users.[29]

III. Development of Doctrine by the Courts and Expanded Specificity in Legislation

The courts exercising their common law authority developed much of the basic tax doctrine in the US. A broad, inclusive statute followed adoption of the income tax amendment to the Constitution authorising the federal government to tax incomes

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26 OECD, "BEPS: Inclusive Framework on Base Erosion and Profit Shifting" (n. 8).

27 Yolanda K Kodrzycki and Eric M Zolt, "Tax Issues Arising from Privatization in the Formerly Socialist Countries" (1994) 25 *Law and Policy in International Business* 609; Vahram Stepanyan, "Reforming Tax Systems: Experience of the Baltics, Russia, and Other Countries of the Former Soviet Union" (IMF Working Paper WP/03/173, 2003), available at https://www.imf.org/external/pubs/ft/wp/2003/wp03173.pdf accessed 18 August 2023.

28 Eg, see Form 1040 for income tax reporting in the US requires taxpayers to report holdings and dealing in cryptocurrencies. Similarly, when it becomes effective in 2024, IIRC §6050I(d)(3) will include cryptocurrency in trade or business cash payment reporting requirements.

29 Orly Mazur, "Taxing the Cloud" (2015) 103:1 *California Law Review* 1. Orly Mazur and Rifat Azam, "Cloudy with a Chance of Taxation" (2019) 22:2 *Florida Tax Review* 500.

without apportionment among the states.[30] Congress enacted income tax statutes including the basic rule of inclusion: "gross income includes all income from whatever source derived."[31] This formulation of inclusion in the income tax base had little additional embellishment when first enacted although it did include examples of inclusion as it does today. Defining the scope of the statute was left to the courts, and they did indeed fill in many details.

A. Realisation

Eisner v Macomber[32] limited an express statutory inclusion of stock dividends in gross income to those that might result in some alteration in the rights of the shareholding taxpayer. If all shareholders received additional shares in proportion to pre-dividend share ownership without the possibility that the dividend might alter proportional voting rights or economic participation, the stock dividend was not income. Congress followed later and codified the interpretation with detailed rules.[33] As a constitutional law decision, *Macomber* created a judicially defined constitutional realisation requirement for inclusion in gross income.[34]

B. Compensation and attribution of income

Several decisions added rules on compensation for services to the basic rule of inclusion in gross income. *Lucas v Earl*[35] held that a taxpayer may assign income from his services to his spouse, but the assignment would be ineffective for tax purposes and the income taxed to the service provider. The decision was unfortunate because it created a tax advantage for those residing in community property states because the income split in such states was by operation of law and a valid shift of income from one spouse to another.[36] States rushed to enact community property laws to enable their residents to enjoy the benefit of income splitting from two sets of marginal rate brackets. Congress finally eliminated the common law/community property law state differential in 1948 with adoption of joint return filing.[37]

Another compensation decision, *Old Colony Trust v US*,[38] established that an employer's payment of the employee's tax obligation under a net salary agreement was income

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30 US Const Amend XVI (1913).
31 IRC §61 is the current statute.
32 *Eisner v Macomber* 252 US 189 (1920).
33 IRC §305.
34 Henry Ordower, "Revisiting Realization: Accretion Taxation, the Constitution, Macomber, and Mark to Market" (1993) 13:1 *Virginia Tax Review* 1. Mark to market taxation of certain positions under IRC §1256, in effect after 1983, the expatriation tax under IRC §877A, and the transition tax under IRC §965 seem to violate the limitation of Macomber. The US Supreme Court held in *Moore v United States* 602 US __ (2024) that IRC §965 is constitutional on grounds other than realisation. The Court's majority determined that Congress has the power to disregard a foreign corporation for tax purposes and tax corporate shareholders directly on the corporation's realised income as the Code taxes the income of S corporations to its shareholders under subchapter S of the Code, the income of partnerships to its partners under subchapter K of the Code, and portions of the income of controlled foreign corporations under IRC §951 et seq. of the Code.
35 *Lucas v Earl* 281 US 111 (1930).
36 *Poe v Seaborn* 282 US 101 (1930).
37 IRC §6013 currently.
38 *Old Colony Trust v US* 279 US 716 (1929).

to the employee. The employee sought to exclude the tax payments because he never had the contractual right to receive the payments directly.

But in the taxpayer favourable case, *Benaglia v Commissioner*,[39] the Board of Tax Appeals, now the Tax Court, held that meals and lodging received by an employee in kind for his family and himself at a Hawaiian resort were not income because the employee and his family received the meals and lodging for the convenience of the employer insofar as the employee was always on call. This decision seems peculiar in conflating benefit to an employer with incidence of taxation to the employee. Nevertheless, Congress later confirmed the court's holding with a statute detailing the rules for exclusion.[40] Another taxpayer-favourable compensation decision interpreting the basic income inclusion statute and its subsequent express application to property received for services[41] opened the way for private equity fund service partners to defer their income on receipt of the interest in the fund and convert the income into tax favoured long term capital gain.[42]

C. Gifts

The Supreme Court committed the decision-making authority to demarcate excludable gifts from includable compensation-like income to the courts as a question of fact.[43] And despite the breadth of the general income inclusion statute, a definitive statement on inclusion of windfalls in income did not arrive until 1955 and also came through the courts.[44]

The legislature asserted increased control over the inclusion of compensation income when it added a specific statutory exclusion for meals and lodging to the Code in 1954.[45] Similarly, Congress added a provision specifying rules and adding bulk and detail to tax law for compensation paid with property other than cash. The statute includes a complex timing rule for those compensation arrangements in which the service provider would forfeit property transferred if the employee or other service provider failed to meet a contractual provision often related to length of service.[46] Even more detailed is the exclusion for compensation in the form of fringe benefits.[47] The statute represents a stark departure from the more general statutory drafting that characterised the early income tax statutes.

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39 *Benaglia v Commissioner* 36 BTA 838 (1937).
40 IRC §119.
41 IRC §83.
42 *Campbell v Comm'r* 59 TCM (CCH) 236 (1990), affirmed in part, reversed in part, 943 F 2d 815, 8th Cir (1991); Revenue Procedure 93-27, 1993-2 C.B. 343. Congress has debated this compensation issue on several occasions but has not succeeded in reversing the conversion outcome. In 2018, it limited long term capital gain to those instances in which the service partner held the partnership interest for at least three years. IRC §1061.
43 *Comm'r v Duberstein* 363 US 278 (1960).
44 *Comm'r v Glenshaw Glass Co* 348 US 426 (1955).
45 IRC §119. See John H McDermott, "Taxation - Federal Income Tax - Meals and Lodging under the 1954 Code" (1955) 53:6 *Michigan Law Review* 871.
46 IRC §83, added to the Code in 1969.
47 IRC §132, added to the Code in 1984. The IRS proposed introducing fringe benefit regulations in the mid-1970s to tax income from various benefits that previously rarely had been taxed. Congress enacted a moratorium on the issuance of fringe benefit regulations in 1977 leaving a period of uncertainty during which the IRS did not seek to collect tax on fringe benefits until Congress enacted the statute in 1984. See, generally, Julia Kalmus, "The Moratorium Is Over: Fringe Benefits under the Tax Reform Act of 1984" (1985) 5:2 *Pace Law Review* 309.

It includes complex definitions and rules of application but nevertheless leaves room for administrative or judicial interpretation within a narrow band of possibilities much like statutes under civil law regimes.

D. Growing legislative specificity

This trend towards ever greater specificity in drafting is clearly visible in the depreciation rules, as a simple rule of allowance for depreciation and wear and tear of tangible property[48] yielded to detailed rules for tangible property. The new rules provided a complex but predictable methodology for depreciation that included a period, method, and convention with variants for special situations and anti-churning rules.[49] The transformation in depreciation eliminated much litigation concerning the useful life of property and the salvage value while enabling subsidisation of investment in durable property through a rapid depreciation tax benefit. The drafting style significantly narrowed the role of the courts in examining facts pertaining to depreciable property.

Since 1981, the detailed and complex tax drafting style has become dominant in the US. Tax practitioners generally advocate for ever greater specificity so that they have certainty in application both in complying with and identifying statutory flaws that they may exploit. Detailed drafting, however, often leaves courts reluctant to address factual patterns in which taxpayers do not follow the statutory outlines in constructing their transactions. When new types of transactions or technologies emerge, the Internal Revenue Service (IRS) and courts may have to await Congressional action before they can address new tax issues while under more general rules both the IRS and the courts could fashion the needed rules. The government would not have to cede a, possibly unjustifiable, victory to taxpayers for lack of the necessary tax rule as occurred recently with cryptocurrency staking. There the government chose to refund the tax to the taxpayer rather than litigate an emerging issue to resolve a controversy for which no specific statute or legal precedent controlled although ready analogies were at hand.[50] The case illustrates how absent statutory guidance, it becomes more difficult for the IRS and courts to use the broad general principles of the previous judicial decisions and rulings to determine outcomes, so that the government and taxpayers are left with uncertainty.[51]

IV. The Constitutional Court in Germany Shaping Tax Law

The number of tax decisions rendered by the German Constitutional Court is considerable. Many reject the structure or rules that the legislature chose. Like common law courts, the Constitutional Court addresses specific cases before other courts but referred

48 IRC §167.
49 IRC §168, added in 1981 and amended on multiple occasions to adjust the tax subsidy.
50 *Jarrett v United States* 79 F 4th 675, 6th Cir (2023) (holding that refund of the tax renders the case moot even if the taxpayer does not negotiate the refund check).
51 More recently, the IRS ruled on staking rewards in a manner contrary to its settlement in Jarrett, n. 50, Revenue Rulings 2023-14, 2023-33 *Internal Revenue Bulletin* 1.

to it because of an underlying constitutional question.[52] The Constitutional Court's decisions reach further than simple application of legislation to sets of facts. The court plays an important role in development of German tax law as the US Supreme Court did in the early years of the US income tax.[53]

While the Constitutional Court conceded that the legislature was free to determine how to provide social welfare assistance, it observed that the basic law (constitution)[54] required a guaranteed subsistence minimum for each citizen.[55] That subsistence minimum requirement led the court to hold that a child supplement combined with an exemption was not adequate to meet that tax free subsistence minimum.[56]

That tax free subsistence minimum was also instrumental in the court's rejection of a legislative limitation on the deductibility of duplicative expenses of maintaining a second household.[57] But the court limited its intervention to average expenses consistent with the subsistence minimum and not a function of the taxpayer's specific and perhaps higher standard of living than average.[58] The Constitutional Court's common law-like activism is reflected in its sweeping language defining its role in shaping the tax law according to fundamental principles:

> The fundamental freedom of the legislature to determine rules applicable to factual configuration, … is limited in the area of tax law and in particular for that of income tax law by two closely related guidelines: the requirement to align the tax burden with the principle of financial ability to pay and by the requirement of consistency. Accordingly, in the interest of equal tax burdens required under constitutional law, the aim must be to tax taxpayers with the same ability to pay the same amount (horizontal tax equity), while (in the vertical direction) the taxation of higher incomes must be appropriate in comparison with the tax burden on lower incomes (citations omitted). Although the legislature has extensive decision-making leeway when selecting the subject of the tax and determining the tax rate, it must, under the requirement that all taxpayers be burdened as evenly as possible when designing the initial tax situation, implement the decision consistently with a sense of equal burdens (citations omitted). Exceptions to such a consistent implementation require a special factual reason (citations omitted).[59]

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52 Bundesministerium der Justiz, "Grundgesetz für die Bundesrepublik Deutschland (Basic Law of the Federal Republic of Germany)" (May 1949), last amended by art.1 G of 19.12.2022 I 2478 (requiring courts to stay proceedings and refer of constitutional questions to the Constitutional Court, available at https://www.gesetze-im-internet.de/gg/BJNR000010949.html accessed 26 August 2023.

53 Henry Ordower, "Horizontal and Vertical Equity in Taxation as Constitutional Principles: Germany and the United States Contrasted" (2006) 7:5 *Florida Tax Review* 259; Bodo Pieroth, "Die neuere Rechtsprechung des Bundesverfassungsgerichts zum Grundsatz des Vertrauensschutzes" (1990) 45:6 *JuristenZeitung* 279.

54 Grundgesetz (GG) arts.1 (human dignity principle), 3 (equality principle).

55 BVerfGE 40,121, 133 (1975).

56 BVerfGE 82, 198 (1990). BVerfGE 87, 153 (1992) (subsistence minimum necessary to make up for indirect taxes on low income individuals).

57 BVerfGE 107, 27, 35 (2002) (dual residence case).

58 *Ibid.*, 48.

59 *Ibid.*, Para 50:
Die grundsätzliche Freiheit des Gesetzgebers, diejenigen Sachverhalte tatbestandlich zu bestimmen, … wird für den Bereich des Steuerrechts und insbesondere für den des Einkommensteuerrechts vor allem durch zwei

The Constitutional Court's decisions have defined limits on taxation rules and have been far reaching. In 1995, for example, repeal of the wealth, inheritance and gift taxes followed from the Constitutional Court's decision rejecting the existing formulation of those laws for failure to determine value correctly and currently in violation of the equality principle.[60] In the specific limitations it imposes, the court acts as a common law-type court shaping the tax law by directing the legislature to modify its enactments in specific ways. The court dampens the impact of its common law-type pronouncements, however, by delaying their effective date of its decisions to permit the legislature to enact the necessary changes in the law without requiring refunds.[61]

V. The European Court of Justice as a Common Law-Type Court

Like the German Constitutional Court, the European Court of Justice (CJEU) examines national tax laws relative to the cooperative principles of the European Union. It renders decisions in the manner of common law courts on a specific controversy before it. The Court tests national legislation having cross-border reach against the EU's governing treaties[62] in a manner analogous to a common law court. It requires national legislatures to modify their tax rules to coincide with overriding principles of the treaties.

For example, in two cases the CJEU shaped the French exit tax as it exercised its authority to determine restrictions on national law in the EU.[63] Despite French legislation imposing an exit tax on the unrealised gains of a taxpayer relinquishing residence in France who relocated to another EU jurisdiction, the CJEU ruled the tax to violate the Treaty of Rome guaranteeing free movement insofar as the facts demonstrated that the taxpayer remained in the EU.[64] But where a similar taxpayer moved to Switzerland, the CJEU held (preliminarily) that the tax was permissible despite similarity between the free movement agreements between France and Switzerland and the Treaty. The broad application in the EU did not apply to Switzerland.[65] More recently, the ATAD encourages more extensive use of exit taxes for corporations changing their residence even within the EU.[66]

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eng miteinander verbundene Leitlinien begrenzt: durch das Gebot der Ausrichtung der Steuerlast am Prinzip der finanziellen Leistungsfähigkeit und durch das Gebot der Folgerichtigkeit. Danach muss im Interesse verfassungsrechtlich gebotener steuerlicher Lastengleichheit … darauf abgezielt werden, Steuerpflichtige bei gleicher Leistungsfähigkeit auch gleich hoch zu besteuern (horizontale Steuergerechtigkeit), während (in vertikaler Richtung) die Besteuerung höherer Einkommen im Vergleich mit der Steuerbelastung niedriger Einkommen angemessen sein muss (citations omitted). Zwar hat der Gesetzgeber bei der Auswahl des Steuergegenstands und bei der Bestimmung des Steuersatzes einen weitreichenden Entscheidungsspielraum, jedoch muss er unter dem Gebot möglichst gleichmäßiger Belastung aller Steuerpflichtigen bei der Ausgestaltung des steuerrechtlichen Ausgangstatbestands die einmal getroffene Belastungsentscheidung folgerichtig im Sinne der Belastungsgleichheit umsetzen (citations omitted). Ausnahmen von einer solchen folgerichtigen Umsetzung bedürfen eines besonderen sachlichen Grundes (citations omitted).

60 BVerfGE 93, 121 (1995) (wealth tax) and BVerfGE 93, 165 (1995) (inheritance tax).

61 Eg, see BVerfGE 87, 153, 178.

62 Treaty on the Functioning of the EU, (n. 7).

63 Daniel Gutmann, "La lutte contre 'l'exil fiscal': du droit comparé à la politique fiscale" *Le Cercle Des Fiscalistes* (2012).

64 *Hughes de Lasteyrie du Saillant v Ministère de l'Économie, des Finances et de l'Industrie* (Case C-9/02), 2004 ECR I-2452.

65 *Christian Picart v Ministre des Finances et des Comptes publics* (Case C-355/16), ECLI:EU:C:2018:184.

66 Council Directive (EU) 2016/1164 (n. 6). Article 5 Exit taxes.

Finnish domestic law allowed shareholders subject to Finnish tax a credit for the withholding tax on dividends that Finnish, but not foreign, corporations pay to their shareholders. The CJEU overrode the Finnish legislation in determining that the EU treaty on free movement of capital required Finland to grant a credit for other EU states' withholding taxes on dividends paid to Finnish shareholders by a corporation resident in those other states. In the case, the other state was Sweden, and the credit was required to be available even though Finland did not collect the corporate tax or the withholding tax that was being credited.[67]

Similarly, the CJEU applied a broad principle of proportionality compelling the UK to grant a corporate deduction to the parent of a non-consolidated foreign subsidiary when those losses became final but could not be used in the subsidiary's country of residence. The loss occurred and could be taken into account in the UK even though the expenditures did not take place in the UK.[68] The CJEU similarly applied a principle of proportionality to allow losses in Denmark for a non-consolidated Finnish permanent establishment that it could have elected to consolidate but did not.[69] In these cases, the CJEU developed the law that a corporation should not have to waste the potential tax benefit of losses under a broad reading of the proportionality principle under the Treaty. In so doing, the CJEU perceived operations within the EU to be independent of national borders.

The CJEU has reviewed several of the European Commission's (EC) decisions on state aid with careful attention to the facts. State aid refers to a competitive advantage provided to a private actor by an EU member state in violation of Treaty on the Functioning of the European Union (TFEU).[70] The TFEU lists various actions that are compatible with the treaty but does not specify all state actions that might violate the treaty. Development of state aid concepts has been left to the EC, subject to review by the CJEU. In several instances the EC has determined that tax rulings are state aid in cases out of the Low Countries, in particular.[71] The CJEU has not concurred in several instances, thereby extending the CJEU's role as a common law type court in development of tax law under the treaty. For example, the CJEU rejected the EC ruling with respect to application of the arm's length principle in the Fiat Chrysler case because the EC failed to take the Luxembourg statute defining arm's length into account in rendering its decision.[72]

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67 *Petri Manninen* (Case C-319/0), (CJEU, 27 September 2004).

68 *Marks & Spencer plc v David Halsey (Her Majesty's Inspector of Taxes)* (Case C-446/03), European Court Reports 2005 I-10837 (CJEU, 13 December 2005).

69 *A/S Bevola v Skatteministeriet* (Case C-650/16) (CJEU, 12 June 2018).

70 Consolidated versions of the TEU and TFEU (n. 7), arts.107, 108.

71 Christopher Bobby, "A Method Inside the Madness: Understanding the European Union State Aid and Taxation Rulings" (2017) 18:1 *Chicago Journal International Law* 186, available at https://chicagounbound.uchicago.edu/cjil/vol18/iss1/5 accessed 27 August 2023. Giulio Allevato, "Judicial Review of the State Aid Decisions on Advance Tax Rulings: A Last Resort to Safeguard the Rule of Law" (2022) 62:2 *European Taxation* 1.

72 *Fiat Chrysler Finance Europe v Ireland* (Joined Cases C-885/19P and C-898/19P) (8 November 2022), available at https://curia.europa.eu/juris/document/document.jsf?docid=269052&mode=req&pageIndex=1&dir=&occ=first&part=1&text=&doclang=EN&cid=2619114 accessed 27 August 2023.

VI. Ambiguation of Tax Law and the Growth of GAARs

While the CJEU operates much like a common law court with authority to determine and define the tax law under the TFEU, ambiguity and uncertainty in taxation is not only a function of the open provisions of the TFEU. Traditional civil law states recognise that tax avoidance opportunities are inherent and unavoidable in domestic tax rules, no matter how carefully the legislature constructs the laws. That acknowledgment has led civil law jurisdictions to follow the common law tradition and turn to general interpretive principles that the jurisdictions embody in GAARs and special anti-avoidance rules. The ATAD endorses the proliferation of GAARs, and recently the EC has looked to adding sanctions for advisers who assist their clients with aggressive tax planning.[73] This section deals with the development of broad doctrines judicially in the US and statutory doctrines in civil law jurisdictions enabling administrators and courts to override statutes to prevent tax avoidance.

Concerning the common law flexibility in developing legal doctrine in the courts and the emphasis on statutes in civil law, Professor Vanistendael wrote:

> Courts in common law countries tend to pay close attention to the facts and exercise more freedom in their legal reasoning. Courts in civil law countries tend to take greater interest in the exact wording of the applicable rule and are generally stricter in their legal reasoning.[74]

Nowhere has the tension between common law flexibility and civil law precision manifested itself more than in the development of taxation. The UK, the US and other countries emerged from a common law tradition where the judiciary had authority to fashion the law. Tax rules as necessary to resolve tax disputes in applying law to the specific facts in a case were made flexible. European states following civil law depended upon their legislatures to enact and modify taxation rules, leaving their courts to play a minor role in applying statutory language. Accommodation to international tax projects to prevent abuse and avoidance has driven the systemic levelling of common and civil law. The US has trended towards a civil law statutory model in taxation with ever more specific statutes to provide predictability in outcomes while civil law countries have relied increasingly on courts to prevent tax avoidance with broad general anti avoidance tools.

In explaining the presence of anti-avoidance rules in civil law jurisdictions, Professor Vanistendael wrote:

> [t]ax laws being general prescriptions, it is inevitable that the legislator cannot foresee all situations in a rapidly changing world, thereby leaving gaps and loopholes in any tax law. (citation omitted) Also, in many cases, the tax law allows

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73 EC Presentation, "SAFE—Securing the Activity Framework of Enablers Platform for Tax Good Governance" (September 2022), available at https://taxation-customs.ec.europa.eu/system/files/2022-09/EC%20presentation%20-%20SAFE%20-%20Securing%20the%20Activity%20Framework%20of%20Enablers.pdf accessed 27 August 2023.

74 Frans Vanistendael, Legal Framework for Taxation (n. 1).

> the taxpayer a choice between different legal alternatives to reach factual objectives that are identical or very similar, but with different tax consequences.[75]

Early in US income tax history, the courts developed several closely related, non-statutory doctrines to assist in resolving tax disputes. The business purpose, substance over form, sham transaction, economic substance, and step transaction doctrines each enabled the courts to deny taxpayers the tax outcome that would correspond to their chosen transactional structure and substitute an outcome that would have accompanied an alternative structure that is more consistent with the underlying business transaction.[76]

The business purpose and substance over form doctrines emerge from *Gregory v Helvering*, a 1935 decision of the US Supreme Court.[77] In *Gregory*, the taxpayer sought to use a broad general, tax deferred reorganisation statute to characterise a distribution from a corporation she controlled as a corporate separation (or divisive) reorganisation followed by a liquidation of one corporation to yield preferentially taxed capital gain rather than an ordinary income, dividend distribution in kind. The Supreme Court rejected the taxpayer's characterisation finding that, while consistent with the statutory language, the transaction lacked a corporate, rather than shareholder, business purpose and re-characterised its tax outcome consistent with its substance, a dividend. The Court disregarded intermediate but unnecessary steps designed to produce a more favourable tax result.

The sham transaction doctrine, another very broad interpretive rule, overlaps business purpose and economic substance and enables the tax collector to argue that the tax outcome of a transaction must follow its ultimate economic outcome where the transactional structure is designed to permit the taxpayer to capture an unintended tax benefit. Certainly, that is what the taxpayer sought in *Gregory*, but *Knetsch v US*[78] is a clearer example of the breadth of the doctrine. In *Knetsch*, the taxpayer borrowed funds from an annuity issuer to purchase a deferred annuity and pay premiums to carry the annuity. A straightforward, simple statute allowed taxpayers to deduct interest without limitation they paid on borrowed funds.[79] The interest paid was deductible, but the internal build-up in the value of the annuity, fundamentally a return on the funds invested in the annuity, was not taxable under a similarly straightforward statute. The build-up supported the annual borrowing to pay the premium but the interest payable on the borrowed funds was greater than the internal build-up, so that economically, the arrangement produced a loss for the taxpayer. However, the interest deduction was quite valuable to the taxpayer who was subject to tax at a marginal rate exceeding 90 percent, so that the tax reduction was much greater than the difference between the interest payable on the borrowed funds at 3.5 percent and the increase in the policy value of 2.5 percent. The transaction was held to be a sham and the interest deduction denied because the annuity combined with the borrowing made economic sense only through its tax savings.

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75 *Ibid.*
76 Joshua D Rosenberg, "Tax Avoidance and Income Measurement" (1988) 87:2 *Michigan Law Review* 365.
77 Gregory v Helvering (n. 11).
78 *Knetsch v US* 364 US 361 (1960).
79 Current IRC §163 is the successor of that statute and has become gradually riddled with detailed and complex limitations on deductibility of interest.

GAARs serve purposes like the various non-statutory, interpretive doctrines that developed in the US during the first half century of its income tax. The statutory formulation of the GAAR tends to emphasise what the legislature would have anticipated when it enacted the statute but does not require the tax administrator to support a conclusion with legislative history to apply the GAAR. For example, the German GAAR[80] permits the tax authority to ignore a transaction when the taxpayer abuses an otherwise permissible legal form or transaction to capture a tax benefit that is inconsistent with what the legislative purpose would have been.[81] A reasonable business purpose for the transaction or structure independent of the tax advantage is a defence to application of the GAAR.[82] The Swedish GAAR similarly permits the tax authority to disregard the taxpayer's transactional structure if the principal purpose for the structure is to capture a tax advantage that would not have been available under a more reasonable structure.[83] The notion that the tax authority may disregard a lawful structure because it yields a tax advantage contrary to what might be anticipated from a statute but fully consistent with the statutory formulation is a significant departure from civil law traditions under which legislation is primary.

A recent deployment of the German GAAR to assist in combatting the Cum-Ex transactions is significant. In one variation of those transactions, two taxpayers met the requirement for a refund or credit of the 30 percent withholding tax on corporate dividends. In Germany, banks were authorised to issue certificates for the withholding tax refund to shareholders owning the underlying shares on the ex-dividend date. A facilitator would sell the shares short to one such refund entitled shareholder before the ex-dividend date and borrow the shares from another refund entitled shareholder to deliver them. On the ex-dividend date, the block of shares would seem to be owned by both the short buyer and the original owner and both would receive a refund certificate thereby doubling the refund. Separation of the tax refund mechanism from the actual withholding facilitated the doubling of the refund. Obvious to everyone was that a double withholding refund made no sense but was possible under the statutory scheme for refunding withholding and the statute itself did not have the necessary safeguards to prevent a double refund.[84]

The US does not have a GAAR but has codified the economic substance doctrine.[85] The codified doctrine does not appear to have the same broad reach as the German and Swedish GAARs insofar as the statute limits its operation only when there is no change in the taxpayer's economic position other than the tax advantage. Other non-statutory interpretive doctrines continue although the taxing authority increasingly frequently has

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80 AO §42 (n. 4).

81 The EC's SAFE proposal uses a similar formulation of imputed legislative intent in its effort to staunch aggressive tax planning. EC Presentation, "SAFE—Securing" (n. 73). The specific formulation for SAFE is: "not aligned with the spirit of the law."

82 AO §42 (n. 4).

83 Lag (1995:575) mot skatteflykt, as amended by Lag (2011:1372) (n. 4).

84 Correctiv, "Cumex Files", available at https://correctiv.org/en/latest-stories/2021/10/21/cumex-files-2/ accessed 20 August 2023.

85 Compare IRC §7701(o) (statutory manifestation of an economic substance doctrine added to the Code in 2010 by the Health Care and Education Reconciliation Act of 2010, Sec 1409, Pub L No 111-152, 124 Stat 1029, 1067 (30 March 2010).

met resistance in court when it seeks to apply them. Absent specific statutory authority to disregard the taxpayer's structure in more recent years, courts have assumed that the legislature could have modified or enacted specific legislation to prevent the taxpayer from gaining a tax benefit. Failure to legislate is the legislature's shortcoming. The court should not do the legislature's job for it.[86] Thus, it seems that some civil law jurisdictions have moved towards broad, general interpretive doctrines for tax administrators and courts to deploy to combat tax avoidance and evasion while the US has retreated from such doctrines in favour of committing the job of preventing tax avoidance to the legislature.

VII. Conclusion: Merging Common and Civil Law for Taxation, the BEPS Developments, and the ATAD and Hybrid Mismatch

As taxation in the US gradually has become more civil law like and moved towards statutorily complex but clearly defined rules, civil law countries have sought flexibility in application of their tax laws to limit tax avoidance and arbitrage. Those civil law jurisdictions have enacted broad statutory overrides that move them towards common law interpretative flexibility as they confront aggressive tax planning. The ATAD[87] embraced GAARs as a critical tool for controlling tax avoidance and applauded the OECD's BEPS projects.[88] It also identified five principal tax planning areas to address, including related entities and transfer pricing, borrowing costs and deductibility, exits and exit taxes to capture unrealised appreciation, controlled foreign company rules, and hybrid mismatches. All the identified areas emphasise the ability of taxpayers to arbitrage differences in tax computations, rates, and rules across jurisdictions.

The extensive BEPS projects seek to staunch tax arbitrage by redirecting taxable income to high tax, developed economies, rejecting longstanding acceptance of respect for taxpayers' chosen business structure and accompanying favourable tax characteristics. The GloBE minimum tax, also referred to as BEPS II, aims to compel low tax jurisdictions to impose at least a 15 percent tax on income without regard to whether the low or no tax jurisdictions have the tax infrastructure needed to impose the 15 percent tax. While 138 jurisdictions have agreed to the minimum tax, implementation in a fully consistent manner remains challenging. Lack of uniform tax rules, however, thwarts any effort to control tax arbitrage.[89] Even if rates become uniform, tax competition may shift to the design of the tax rules and the practicalities of collection. The uniform rate may serve only to allow developed economies to capture more tax revenue at the expense of those economies that previously used a very low rate to capture much needed investment.

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86 *South Dakota v Wayfair* 585 US 162 (2018), is an exception. In *Quill Corp v North Dakota* 504 US 298 (1992), the Court invited Congress to change the rule on collection of remote use tax by sellers only to change the rule itself when Congress failed to act.

87 Council Directive (EU) 2016/1164 (n. 6).

88 OECD, "BEPS: Inclusive Framework on Base Erosion and Profit Shifting" (n. 8).

89 Henry Ordower, "Uniform International Tax Collection and Distribution for Global Development, a Utopian BEPS Alternative" (2021) 12:2 *Columbia Journal of Tax Law* 126.

Absent uniform rules, no country is immune from offering tax arbitrage opportunities and even actively engaging in tax competition to capture business and investment. At the simplest level, a rule as basic as the realisation requirement for inclusion provides an opportunity to shift assets to jurisdictions permitting tax deferral longer than others. The basis step up at death rule in the US encourages taxpayers with large amounts of appreciated assets to change their residence to the US in their old age so that gain that would inhere in their assets disappears at their death.[90] And many countries, the US in particular, continue to rely on their tax system to deliver subsidies and incentives rather than constructing a separate and politically more transparent mechanism for those subsidies.

Nevertheless, as this article illustrates, taxation is indeed hybrid between civil and common law, public and private law. The essential process of making tax uniform has begun and is facilitated by the hybrid nature of tax. Basic distinctions between common and civil law retreat in importance. Nations regularly borrow tax concepts and design from other nations so that tax systems and rules tend to converge. The ubiquity of tax draws many thoughtful, resourceful, and creative people to the tax discipline. Tax hybridity should look to harness that creative power to make tax work towards transparent, uniform rule-making free from opportunities for arbitrage and competition, leaving competition to productive creativity.

90 IRC §1014.