Federal University of Ceará

From the Selected Works of Hugo de Brito Machado Segundo

March 25, 2013

Still on the repayment of indirect taxes

Hugo B Machado

Available at: https://works.bepress.com/hugo_machado/1/
STILL ON THE REPAYMENT OF ‘INDIRECT’ TAXES’

Prof. Dr. Hugo de Brito Machado Segundo
Professor of Tax Procedural Law and Philosophy of Law at Federal University of Ceará (Brazil)
Head of the Graduate (Master’s and Doctoral Programs) Department
hugo.segundo@ufc.br

Abstract: The repayment of indirect taxes raises questions in many parts of the world, mainly because of the so called “passing-on defense”. Brazilian Courts has given inadequate treatment to this subject, which, in fact, denies the judicial review of the tax relationship, violating the the idea of rule of law. European Court of Justice has different concerns when examining the matter, recognizing that the shift of the tax burden is very difficult to determine and measure. It happens in relation to all taxes, to a greater or lesser extent, and should be taken into consideration by the legislature in fixing the rates of taxes on certain products, as a matter of tax policy, but not on individual relationships, to deny the taxpayer rights, as the repayment of ultra vires taxes, especially because it would be contradictory to do so and at the same time, deny such rights also to the ultimate consumer who eventually supported the tax burden. The price paid by consumers for goods and services, although probably higher because of taxes, cannot be confused with these taxes, so the repayment of the latter should not be hindered or embarrassed because of a (supposed) shift of tax burden.

Keywords: Indirect taxation. Restitution of ultra vires taxes. European Court of Justice. Tax shifting. Burden of tax.

1. Introduction

There are several discussions surrounding the issue of repaying taxes unduly paid, especially those regarded as ‘indirect’. This is because Tax Authorities often create obstacles or difficulties to this kind of tax restitution, in addition to the usual impediments imposed to tax refunds in general. It is interesting to note that such difficulties are (or have already been) created by Tax Authorities in several different countries. The main difference is actually in how taxes are regarded by Courts in charge of reviewing conflicts arising from them. Ultimately, it is the Courts’ opinion that defines how ‘indirect’ tax restitutions are addressed in each country.

For this reason, in this study I intend to return to the issue of repaying indirect taxes. I will initially conduct a comparative analysis of legal precedents, basically

---

2 Problems relating to indirect taxation have been previously analyzed by the author of this paper, in the light of Brazilian legal precedents and in a more comprehensive manner (involving an examination of its treatment
comparing the opinions of the Brazilian Federal Supreme Court (Supremo Tribunal Federal – STF) and the Brazilian Superior Court of Justice (Superior Tribunal de Justiça – STJ) and the Court of Justice of the European Union (ECJ). I will also look into decisions handed down by STJ in 2012 regarding the position of electricity consumers in claims that attempt to question the State Goods and Services Tax (ICMS) levied on consumed electricity in order to assess which treatment should be given to ‘de facto taxpayers’ of such taxes.

This comparative legal precedent analysis will allow us to reexamine the matter, especially with respect to possible repercussions of the economic burden of taxes on third parties, to the burden of proof and its possible legal consequences. The main distinction in this case does not lie so much in what scholars state about the matter, but rather on the opinion of surrounding courts. In Europe, for example, there is a noticeable difference between the position taken by national courts and that accepted by the European Court of Justice (ECJ). Maybe this is the result of the ECJ being less subservient to the Taxing Authority of each member state, or of more evident concern with commanding respect to community rules violated by member states. Furthermore, if problems faced by different countries are the same, there is no reason for one not to become acquainted with the solution found by others. After all, the best solutions are more likely to be found when there is a greater and more intense exchange of ideas.4

I would like to point out that this paper, in regard to the analysis of European Court of Justice Precedents, is the result of post-doctoral research conducted in 2012 in the Wirtschaftsuniversität in Vienna, at the Institut Österreichisches und Internationales Steuerrecht, under the supervision of Professor Dr. Michael Lang. Therefore, I would like to take this opportunity to thank Professor Lang and all those who are part of the Institute5

---

5 Especially Professor Pasquale Pistone, Renée Pestuka and the colleagues César Alejandro Ruiz Jiménez, Daniel Fuentes, Felipe Vallada, Sebastian Pfeiffer, Pernille Jessen and Yinon Tzubery.
for being so receptive and supportive; without you this small study would not have been possible.

2. What are indirect taxes?

Since the discussion here addresses the restitution of taxes regarded as ‘indirect’, it is only fitting to start by defining or identifying them. This pertains to an ancient classification made centuries ago by economists and financiers. Stuart Mill discusses the matter in Principles of Political Economy (1848) in the following terms:

A direct tax is one which is demanded from the very persons who, it is intended or desired, should pay it. Indirect taxes are those which are demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another: such as the excise or customs. The producer or importer of a commodity is called upon to pay a tax on it, not with the intention to levy a peculiar contribution upon him, but to tax through him the consumers of the commodity, from whom it is supposed that he will recover the amount by means of an advance in price.

Based on this idea, to this day it is said, as if one were discussing something extremely simple, that indirect taxes are those in which the taxpayer legally defined as such, also known as ‘de jure’ taxpayer, transfers or shifts the tax burden to a third party who supports it economically and is therefore called 'de facto' taxpayer. Direct taxes, on the other hand, are those taxes which are not transferred or shifted; therefore, the same person embodies the notions of 'de facto' and 'de jure' taxpayer. Some also simplistically state that taxes levied on property and income are direct, while taxes levied on consumption are indirect.

The problem is that the economic criterion, used by Mill (and so many others), does not allow for classifying taxes into a category or another, for all of them may have their burden shifted to a third party, according to the circumstances, when corresponding prices are set. As every cost component, they are taken into account and influence the setting of prices, whether they are direct or indirect. Stuart Mill himself, by the way, soon

---

6 There are records of it being used in the Middle Ages and even before that, since the distinction arose from another classification that is even older and which separates taxes into real and personal. On this topic see NEVIANI, Tarcísio. A Restituição de Tributos Indevidos, seus problemas, suas incertezas. São Paulo: Resenha Tributária, 1983, p. 61.

after addressing classification, acknowledges that income tax, despite being often considered direct, may cause a manufacturer or seller, in the condition of taxpayers, to increase prices and respectively shift their burden onto third parties.\(^8\)

Nonetheless, this classification is still largely used to this day. And if one intends to use it, may he do so by construing it in a less imperfect fashion, that is, not based purely on economic criteria or clinging to an alleged (and effective) shift of the economic burden alone. In fact, one should regard as indirect taxes which burden events that, strictly speaking, disclose the ability to pay taxes of persons who are not legally defined as taxpayers, even though they take equal part in such events. That is the case of taxes that are usually levied on consumption, which are graduated in order to achieve consumers’ taxpaying ability, and not that of manufacturers or sellers. That is why their tax rate is usually graduated based on how essential the encumbered goods are; this is done taking into account the taxpaying ability of whoever consumes the merchandise, and not who manufactures or sells it.\(^9\)

In summary, the economic reality in which the tax is levied seems to be a less imperfect criterion on which to base a classification.\(^10\) Such is the guidance provided by the following lesson given by Lapatza:

Legislators will usually attempt to levy taxes on those who are able to pay them, on whoever is economically able to afford them.

An individual’s economic ability depends on their wealth, and this becomes directly or indirectly clear by the ownership of property or earning of income.

In that sense, taxes levied on income and property are indirect taxes, since they encumber wealth in itself, considered directly and indirectly.

However, an individual’s wealth can manifest itself indirectly through its use; and a tax may be levied on this use.

The subject matter of indirect taxes is precisely indirect manifestations of economic capacity, such as circulation or wealth consumption.\(^11\)

---


\(^9\) Products in the basic food basket, which are among the top items consumed by persons whose taxpaying ability is limited, are usually subject to a lower tax burden than luxury or costly products that are consumed by richer individuals, as a rule. And this is regardless of whether products from the basic food basket are manufactured by a large company whose taxpaying ability is immense, or whether the luxury product is manufactured by a modest business, which reveals that a duty’s aimed taxpaying ability is that of consumers and not of taxpayers legally defined as such.

However, it is irrelevant to criticize the classification at this point. Such criticism may be made afterward. For the time being it is important to identify which taxes are regarded as ‘indirect’, a task so difficult it is proof of how frail the classification itself is. Incidentally, it is curious to notice that, at least in Brazil, legislators have never taken the risk of pointing out or listing which taxes would be ‘indirect’. Even Article 166 of the Brazilian National Tax Code (Código Tributário Nacional – CTN), which according to legal precedents is applicable to such taxes, does not list them and merely mentions vaguely ‘taxes which allow, by their nature, shifting the financial burden’. Why did legislators not point them out?

What matters without immediately entering into this discussion is that according to Superior Court of Justice precedents, the following are regarded as ‘indirect’, in Brazil: ICMS (Tax on the Circulation of Goods and on Services of Interstate and Intermunicipal Transportation and Communication), IPI (Tax on Manufactured Products) and ISS (Municipal Services Tax), the latter when charged on non-fixed amounts, namely those proportional to the price of the corresponding service. There are no clear grounds that explain why those taxes and not others, such as CIDE-Combustíveis (Contribution of Intervention in the Economy – Fuels), COFINS (Contribution to Fund Social Security), IRPJ (Corporate Income Tax) on presumptive profit, those calculated and paid under the National Simples system, etc. For the time being, it is relevant to ascertain the treatment given to those taxes which are simplistically regarded as ‘indirect’.

13 ‘Article 166 of the CTN is only applicable to indirect taxes, that is, those that are explicitly embedded into prices, such as ICMS, IPI, etc.’ (STJ, AI 452.588/SP, DJ of 5/4/2004, p. 205)
14 “1. ISS is a tax type that may work as a direct or indirect tax, depending on each concrete case. 2. As a rule, ISS’s tax base is the price charged for a service, under the terms of article 7 of Supplementary Law 116/2003, in which case the duty becomes an indirect tax, allowing the financial burden to be shifted to the service buyer. 3. It is necessary, in this case, to provide evidence that the duty’s financial burden has not been shifted, under the terms of Article 166 of the CTN. […]” (STJ, 1.st Panel, Internal Interlocutory Appeal in Appeal 692.583/RJ, judgment passed on 11/10/2005, DJ of 14/11/2005, p. 205, rep. DJ of 28/11/2005, p. 208). An examination of the entire contents of the appellate decision reveals that the situations where ISS is allegedly ‘indirect’ are those where its tax base is the price charged for a service, applying Article 166 of the CTN. However, in cases where ISS is levied on fixed amounts, such as partnerships owned by self-employed individuals (Decree-law 406, Article 9.º, §§ 1.º e 3.º), its nature is ‘direct’ and Article 166 is not applicable, because ‘there is no connection between services provided and the tax base of the municipal duty; it is inappropriate to consider that the tax burden has been shifted and consequently to apply Article 166 of the CTN’ (STJ, REsp 724.684/RJ, j. on 3/5/2005, v. u., DJ of 1.º/7/2005, p. 493).
3. Impediments Posed by Tax Authorities to Indirect Tax Restitutions

Brazil’s Tax Authority is known for raising objections to indirect tax restitutions. It claims that when taxpayers sell merchandise whose price already includes the tax burden, they have already been duly restituted or reimbursed. If the payment of the tax is deemed invalid, restituting the taxpayer would cause him to enrich unjustly, since this would see him being reimbursed twice: first by the final consumer, who paid the tax embedded in the price, and second when the Tax Authority returns the unduly paid tax. In this case the tax has not been ‘actually’ paid by the taxpayer who demands restitution; therefore, it should not be returned to him, even if it is admittedly unjustified.

This is what English-speaking countries have come to know as a passing-on defense\textsuperscript{15}. It has been used in fields other than tax law, such as in antitrust legislation.\textsuperscript{16} However, in this study we will only look into its use within the sphere of tax law and whether or not Courts have been receptive to it.

Naturally, allowing a State to keep a sum paid for undue taxes equally implies unjust enrichment by that State. However, tax authority reasoning states that it would be preferable to have the state grow richer rather than private persons, for the former represents collective interests.

As explained above, this argument has not been used by the Brazilian Tax Authority alone. It is or was used in the European Union, the United Kingdom, Canada, Australia, the United States and in some other countries. Therefore, it is interesting to examine how Courts in each of those places considered the use of passing-on defense, so that it is possible to undertake a comparative analysis of the arguments they used and the concerns they voiced.

4. Opinions in Brazilian Legal Precedents

4.1 STF Precedents from the First Half of the Twentieth Century

\textsuperscript{15} Or ‘defence’ with ‘c’ in British English.
The *passing-on defense* has been used for a long time by the Brazilian Tax Authority. There are records of it being cited – in reports and in dissenting opinions in appellate decisions handed down by the STF – in the early years of the twentieth century. Curiously, the Federal Supreme Court emphatically rejected it. That defense would be accepted in appellate decisions handed down by Appellate Courts and eventually in one STF opinion or other, but it was always refuted by the majority in Court.

Most Justices at the time had a clear view of two distinct relationships: on the one hand, the private relationship established between seller and consumer; and on the other hand the Public Law relationship between seller and Tax Authority. In addition, Justices particularly acknowledged that the fact that the second relationship was invalid had absolutely nothing to do with the first. The following excerpt from Justice Laudo Camargo’s opinion, handed down in the judgment of RE 3.051 in 1938, is a fine example of that. Rejecting the Tax Authority’s thesis that, because undue taxes were ‘embedded in prices’, taxpayers could not be restituted for them, Justice Camargo stated that the *acciipiens* has nothing to do with the *solvens’* businesses. The latter, ‘by selling merchandise he owns for one price or another, with a large or small profit, is exercising a right which has nothing to do with the former’s obligation to not take as his own that which belongs to another.’

4.2 STF Precedents from the Second Half of the Twentieth Century

The Tax Authority insisted on using this thesis, though, and it ended up being accepted eventually by the Federal Supreme Court. This confirms the saying: ‘constant dropping wears the stone’. Maybe by misguided using civilist categories, in addition to their superficial knowledge about economics and public finances, Justices started to accept that tax restitutions aimed to make up for ‘harm’ caused by undue taxes; such harm had already been ‘offset’ in cases where the tax had been ‘shifted’ by the taxpayer to a third party. If the taxpayer has already ‘recovered’ the money paid in taxes by receiving compensation for merchandise, granting him a tax restitution, even in the case where

---

payment was undue, would be tantamount to awarding double compensation and this would equal unjustified enrichment.

It is curious to notice that costs may or may not have a repercussion on prices. Such repercussion may only partially occur, and in this case even if the passing-on defense thesis is accepted a tax repayment could not be entirely denied. On the other hand, it is undeniable that shifting the burden is a fact that terminates or bars a plaintiff’s right to file a claim for a tax refund, and the Tax Authority usually responds to it as the defendant. Therefore, at first the burden of proof that shifting has occurred, if resorting to it is relevant, would befall the Tax Authority and not the plaintiff, in accordance with the didactic text of Article 333, I, of the Brazilian Code of Civil Procedure Law (Código de Processo Civil – CPC). However, none of this was taken into account by STF Justices, who not only started to always presume that shifting occurred with respect to particular taxes, but who also assumed it was always in full, placing the impossible burden of proof on the taxpayer, in reverse.19

It is a fact that if the tax is undue, allowing the Tax Authority to keep it would imply unjustified enrichment. There is no denying this. However, as explained before, the Tax Authority's argument which finally prevailed in the STF bypasses this difficulty by appealing to the idea of 'public interest', adding that, by having taxpayers enrich on the one hand, and the Tax Authority on the other hand, the latter would be preferable since this would benefit the entire society. There are records of this 'reasoning' in favor of the state’s unjustified enrichment, for instance, in an opinion handed down by Justice Victor Nunes Leal in the judgment of RE 46.450 in 1961. It would later rely on the support of several well-respected scholars.20

20 ‘The situation is such that, if there are no legal grounds to support the State in case it has received undue sums from taxpayers who have shifted the financial burden to third parties, there are also no legal grounds that would allow the latter, as taxpayers who have not provided evidence that they took on the burden, to claim restitution. And in the absence of grounds on both sides, the crucial principle according to which public interests are above private ones should prevail, and the sums should be added to the State’s assets.’ (CARVALHO, Paulo de Barros. Curso de Direito Tributário. 12th Edition. São Paulo: Saraiva, 1999, p. 419). On that topic, see: TORRES, Ricardo Lobo. Curso de Direito Financeiro e Tributário. 11th Edition. Rio de Janeiro: Renovar, 2004, p. 293; CAPRILLES, Theo. On why EU stand on the passing on defence equates to enriching the unjust. Available online at http://lup.lub.lu.se/luur/download?func=downloadFile&recordOId=2006260&fileOId=2006296, p. 21.
Therefore, although initially rejected, the *passing-on defense* thesis became firmly established in legal precedents, culminating with the publication of Precedent 71 of the STF, which states: ‘although unduly paid, indirect taxes are not to be restituted’.

Some time later the Federal Supreme Court noted that in certain cases even taxes regarded by the Court as ‘indirect’ had not been – and could not have been – shifted to third parties. That is what occurred, for instance, in situations where the price of merchandise was controlled by the Government and subject to listing, when the creation of the tax later regarded as undue *was not* followed by changes in corresponding prices. Those situations led the Court to establish exceptions to when Precedent 71 should be applied; nevertheless it was not cancelled. Its contents were merely ‘clarified’ by Precedent 547, according to which ‘taxes unduly paid are to be restituted when a court ruling acknowledges that the 'de jure' taxpayer has not recovered from the ‘de facto’ taxpayer the respective ‘quantum’’.

It should be noted that the understanding ratified in STF Precedent 547 corresponds overall to what is confirmed by Article 166 of Law 5.172/66 (Brazilian National Tax Code – Código Tributário Nacional – CTN), according to which ‘repayments for taxes which, due to their nature, allow for shifting the respective financial burden shall only be awarded to those who can provide evidence that he took said burden, or, if he shifted it to a third party, that he is expressly authorized to receive such a restitution’. It is also worth noting that Article 166 of the CTN came after the understanding consolidated in the abovementioned precedents; one may say it is a consequence of such precedents. This is because although they were published after the CTN, court decisions that generated its publication arose at least twenty years prior to that.

In any case, this understanding, accepted by the STF, was ratified by the Superior Court of Justice (STJ) which, after the 1988 Federal Constitution, was granted the power to review, at last instance, issues pertaining to the interpretation of infra-constitutional legislation (CF/88, Article 105, III).

---

21 With respect to this issue, in his book published in 1971 Hugo de Brito Machado lists other situations where ‘it is clear that the tax unduly paid has not been shifted. That occurs, for example, when a mistake is made when filling out the tax collection payment slip; or when the duty assessed is summed; or even when the operation which initiated the taxable event is undone’. MACHADO, Hugo de Brito. *O ICM*. São Paulo: Sugestões Literárias, 1971, p. 153.
4.3 STJ Legal Precedents Regarding 'de jure' Taxpayers

The main issue addressed by the Superior Court of Justice (Superior Tribunal de Justiça – STJ) when construing and applying Article 166 of the CTN consisted of knowing which taxes ‘allow for shifting the respective tax burden, by nature’. This is because the Tax Authority would use the passing-on defense based on that article in claims for restitution of undue charges regarding practically all kinds of taxes, namely, income tax, social security contributions on payrolls etc. Since the article does not specify which taxes it applies to, and since every tax, in principle, may have its burden shifted to third parties, the problem was raised as a preliminary issue in appeals for practically all claims for undue tax repayments.

When reviewing such claims the STJ settled upon the understanding that Article 166 of the CTN would be applicable to the restitution of ICMS, IPI and non-fixed ISS, three taxes regarded as ‘indirect’ because they are levied on consumption. Although there is not always clear reasoning in judgments about the reasons why those taxes and not others are regarded as ‘indirect’, Hugo de Brito Machado clarifies, in this point, that the STJ seems to follow the doctrine of Marco Aurélio Greco, for whom Article 166 includes hypotheses of taxes whose taxable event, due to its peculiarities, binds two persons who find in it an element of approximation. In other words, indirect taxes are those whose taxable event is a ‘relationship’, one should say an operation or a transaction, and whose tax base, for this very reason, is the sum for that operation or transaction. Therefore, since those relationships, operations or transactions have two poles or parties; one of them is chosen by legislators as the taxpayer and has the means to shift the tax burden to the other when setting the price for the transaction. This may explain, for instance, the reason why ISS is regarded as indirect when levied on the amount charged by a service, but is regarded as direct when calculated based on the number of authorized professionals in a company formed by self-employed individuals.

---

23 As per, e.g. EREsp (Appeal Against Divergent Decision in Special Appeal) 699.292/SP, which recognizes the ‘indirect’ nature of ICMS.
26 "1. ISS is a tax type that may work as a direct or indirect tax, depending on each concrete case. 2. As a rule, ISS’s tax base is the price charged for a service, under the terms of article 7 of Supplementary Law.
The same grounds provide that income tax and employer social security payroll contributions are regarded as ‘direct’ taxes, not subject to Article 166 of the CTN.

As for social security payroll contributions, there are two aspects worth noting.

The first pertains to the introduction of norms expressly containing *passing-on defense* in ordinary legislation, with the clear aim of ‘protecting’ public funds from the effects of STF decisions which considered unconstitutional social security contributions on payments made to self-employed persons and company managers, which would not be subject to the concept of ‘payroll’ originally included in Article 195 of the 1988 Federal Constitution (CF/88). Indeed, with the clear aim of not repaying the tax which is admittedly unconstitutional, the Government passed Law 9.032/95, which included in Article 89 of Law 8.212/91 a paragraph that read as follows:

§ 1º Restitution or compensation for contributions made by a company to the National Institute for Social Security (Instituto Nacional do Seguro Social – INSS) shall only be admitted when, by their nature, costs pertaining to merchandise or services rendered to society have not been shifted.

As we will discuss below, something similar occurred in the European Community (EU), in Austria.

Another curious aspect, still with respect to the *passing-on defense* in relation to social security payroll contributions, is that the STJ ‘refrained from applying’ the abovementioned legislation for considering that such taxes are not ‘indirect’ and are not subject to the provisions of Article 166 of the CTN; however, Article 89, § 1.º of Law 116/2003, in which case the duty becomes an indirect tax, allowing the financial burden to be shifted to the service buyer. It is necessary, in this case, to provide evidence that the duty’s financial burden has not been shifted, under the terms of Article 166 of the CTN. [...][STJ, AI 692.583/RJ, judgment passed on 11/10/2005, DJ of 14/11/2005, p. 205, rep. DJ of 28/11/2005, p. 208]. An examination of the entire contents of the appellate decision reveals that the situations where ISS is allegedly ‘indirect’ are those where its tax base is the price charged for a service, applying Article 166 of the CTN. However, in cases where ISS is levied on fixed amounts, such as partnerships owned by self-employed individuals, it takes on a ‘direct’ nature and Article 166 does not apply, according to a decision in the judgment of Resp 724.684/RJ, judgment handed down on 3/5/2005, v.u., DJ of 1/7/2005, p. 493.

116/2003, in which case the duty becomes an indirect tax, allowing the financial burden to be shifted to the service buyer. It is necessary, in this case, to provide evidence that the duty’s financial burden has not been shifted, under the terms of Article 166 of the CTN. [...][STJ, AI 692.583/RJ, judgment passed on 11/10/2005, DJ of 14/11/2005, p. 205, rep. DJ of 28/11/2005, p. 208]. An examination of the entire contents of the appellate decision reveals that the situations where ISS is allegedly ‘indirect’ are those where its tax base is the price charged for a service, applying Article 166 of the CTN. However, in cases where ISS is levied on fixed amounts, such as partnerships owned by self-employed individuals, it takes on a ‘direct’ nature and Article 166 does not apply, according to a decision in the judgment of Resp 724.684/RJ, judgment handed down on 3/5/2005, v.u., DJ of 1/7/2005, p. 493.

27 ‘The Superior Court of Justice has settled its understanding that because the additional income tax is a direct duty, it is not subject to shifting and it is not necessary to produce proof that the tax has not been shifted to the de facto taxpayer’. Therefore, for ‘a restitution for sums unduly paid on pretence of additional income tax, Article 166 of the CTN, which addresses indirect taxes, is inapplicable (STJ, 2.ª T., Resp 198.508/SP, judgment handed down on 8/3/2005, DJ of 16/5/2005, p. 276)

28 ‘The 1º Panel of the STJ, when handing down a judgment in Appeal Against Divergent Decision in Special Appeal 189.052/SP, on 12/3/2003, rejected the need for producing evidence that the burden mentioned in Article 166 of the CTN was not shifted, with respect to social security contributions. The Court’s understanding was that a direct tax is not subject to having its financial burden shifted’ (Resp 529.733/PE, DJ of 3/5/2004)
8.212/91 was not formally declared unconstitutional, in clear violation of Article 97 of Brazilian Federal Constitution (CF/88). This is not unusual in Brazilian Courts, so much so that it has led the STF to publish later Binding Precedent 10, according to which ‘Decisions handed down by panels which fully or partly limit the incidence of a law or normative act of the government, even though they do not expressly declare it unconstitutional, violate the full bench rule (CF, Article 97).’

One way or another, what matters is that the criterion used by the STJ to separate direct taxes from indirect ones is not so clear as it seems. Indeed, why not submit the Property Conveyance Tax (Imposto de Transmissão Onerosa Inter Vivos de Bens Imóveis –ITBI) to it as well? And CIDE-combustíveis? And COFINS and PIS? And Income Tax levied on revenue when based on presumptive profit? On the other hand, even the burden of indirect taxes is not always shifted to prices and, more importantly, despite being indirect, they are legally paid by taxpayers and only economically paid by consumers, the so-called 'de facto' taxpayers. Such criticism will be resumed later, especially after we examine the treatment that the European Court of Justice (ECJ) gave to the same issue.

In summary, despite the fact that the STJ has ‘defined’ to which taxes Article 166 of the CTN applies, it has not delved deep into the discussion regarding the shifting of the tax in itself and, just as the STF, it always presumes the tax burden is fully shifted. Therefore, it requires the so-called ‘de jure’ taxpayer, as a condition to granting it active ad causam legitimacy, to provide evidence that the tax burden has not been shifted, or that the ‘de facto’ taxpayer has authorized him to claim a restitution. Since obtaining that evidence is practically impossible, as well as identifying and locating ‘de facto’ taxpayers so they may provide that ‘authorization', restitution of an indirect tax, even when it has been unduly paid, rarely takes place.

One could say, in defense of the position adopted by the STJ, that it was merely applying Article 166 of the CTN. If that provision imposes an impossible condition for repaying an unduly paid tax, this is unconstitutional; it would raise another issue to be ultimately addressed by the STF and not by the STJ. It so happens that it is possible to understand Article 166 of the CTN as applicable only to those taxes for which the law lists more than a single taxpayer, or places more than one person in the taxpayer end of the tax relationship. That is the case of charges, or better, tax obligations (which may pertain to any type or subtype of tax) that have more than one taxpayer (e.g., property owned by
more than a person, joint and several debtors of Municipal Real Estate Tax - IPTU by way of Article 124, I, of the CTN) or taxpayers and tax-responsible persons. It should be noted that the law itself lists a number of debtors or taxpayers. In such cases both may discuss the terms of the legal relationship to which they are parties; however, if the tax is paid it should be reasonably restituted to the one who has effectively (notice the difference! - in any case, legally) paid it.

The STJ has also been applying Article 166 of the CTN in such cases; for this reason the Court could have considered that the article applied to such cases only, in an interpretation in conformity with the Constitution that would not be outside its roles (even so because it is ultimately a Court that also has the power to diffusively control constitutionality, as long as it complies with Article 97 of the CF/88). This point will be readdressed in the final section of this article.

4.4 STJ Legal Precedents Regarding ‘de facto’ Taxpayers and its Oscillations

Along with the discussion about whether the ‘de jure’ taxpayer could legitimately demand restitution for unduly paid taxes, and even as a consequence of answers to this matter provided in legal precedents, the question was raised of whether the ‘de facto’ taxpayer could claim such a repayment. Indeed, if the ‘de facto’ taxpayer has the authority to authorize the ‘de jure’ taxpayer to demand a restitution, why could he not do so on his own behalf? If the reasoning for denying a repayment to the ‘de jure’ taxpayer is the fact that he allegedly shifts the tax to the ‘de facto’ taxpayer, who then would have ‘truly’ taken on the burden of the tax, there is nothing more logical than acknowledging the latter’s can legitimate claim a restitution.

For a long time when reviewing such claims the STJ recognized that the ‘de facto’ taxpayer had legitimacy; because it was presumed that he had suffered the shift, in theory

---

29 ‘TAX LAW. FUNRURAL [Social Security Fund for Rural Workers]. ACTIVE AD CAUSAM LEGITIMACY OF PURCHASER OF RAW MATERIALS FROM RURAL PRODUCERS. ARTICLE 166 OF THE CTN. PRECEDENTS. APPEAL DENIED. 1. ‘This Court’s legal precedents have settled on the opinion that the legal entity that purchases rural products is the tax-responsible person in charge of collecting taxes to FUNRURAL on the commercialization of agricultural products; the legitimacy of such legal entities is limited to questioning the lawfulness or constitutionality of the duty, but does not include claiming restitution or compensation for the tax on their own behalf, except when the conditions in Article 166 of the CTN are met’ (REsp 961.178/RS, DJe 25/05/09). 2. Internal interlocutory appeal denied’. (STJ, AI 198.160/PI, judgment handed down on 09/10/2012, DJe 16/10/2012)
he did not have to prove it. Such decisions pertained basically to electricity consumers and buyers of products on which IPI was levied.

However, in 2010 this understanding changed and the Court also started denying the ‘de facto’ taxpayer legitimacy to claim repayments\(^{30}\). After that it became even more difficult for a person to obtain restitution for taxes regarded as indirect.

The interesting aspect of this issue is that decisions which changed legal precedent to deny legitimacy to ‘de facto’ taxpayers were based on premises that contradicted the thesis generally accepted within the STJ that Article 166 of the CTN would be applicable to those taxes and, therefore, the ‘de jure’ taxpayer could not obtain that repayment either, as a rule. Indeed, decisions make reference to the opinion of authors that claim that Article 166 is unconstitutional or, in the best case scenario, it is inapplicable to so-called ‘indirect’ taxes, a classification they strongly oppose.

Therefore, in summary, the STJ started adopting a reasoning to deny legitimacy to the ‘de jure’ taxpayer, based on the indirect nature of ICMS, IPI and ISS; and on the legal relevance of ‘shifting’ the burden to the ‘de facto’ taxpayer. It also adopted completely opposite reasoning to also deny legitimacy to the ‘de facto’ taxpayer, based on the fact that the abovementioned shift of burden would be legally irrelevant and on the weakness of the classification of taxes in direct and indirect. What is worse, no reference was made to the fact that the STJ itself, for years on end, accepted the opposite understanding, not even to explain the reasons why legal precedents were changing.

Needless to say that this line of thought, in addition to being contradictory, clearly and directly violates the fundamental guarantee of access to justice (judicial control - CF/88, Article 5.°, XXXV), for it allows a violation of taxpayers’ rights, caused by unduly charged taxes, to remain completely immune to judicial analysis.

At a later time, maybe after becoming aware of criticism received from the academic community and cautioned of the negative effects of its understandings surrounding indirect taxes regarded as a whole, the STJ made an exception for electricity consumers only, considering the peculiar nature of the relationship between them and utility companies and how the amount charged for electricity tariffs is defined. It should be noted that the understanding was not entirely modified; the Court merely clarified that it

\(^{30}\) STJ, REsp 1147362/MT, DJe of 19/08/2010.
was not applicable to claims regarding to electricity, although previous decisions involving electricity consumers suggested otherwise.\textsuperscript{31}

This change in legal precedents created a few paradoxical situations, which maybe only make it clearer how wrong is the treatment given to indirect taxes in Brazil. Indeed, during the long period in which the STJ acknowledged the legitimacy of electricity consumers, many of them filed claims questioning ICMS levied on consumed electricity. They not only demanded a tax repayment; they also required charged amounts to be corrected for the future. Many of them obtained preliminary injunctions, ratified by judgments and Appellate Court decisions, which suspended the enforceability of those amounts, which should be extinct when an unappealable judgment was handed down (CTN, Article 156, X). When those actions reached the STJ, the Court changed the, until then, general understanding in its legal precedents and started denying legitimacy to de facto taxpayers. The consequence was that many of the abovementioned claims were dismissed without prejudice, which created a contradictory situation: from whom should the Tax Authority collect 'past due’ amounts, unpaid because of the preliminary injunction?

If its intention was to collect the amounts from utility companies, they could rightfully claim that they did not collect the amounts from electricity consumers, in compliance with a court order, and could not be compelled to pay them now. If its intention was to collect the amount from consumers, they would be put in the unusual position of taxpayers of a charge they could not legally contest because they were not its… taxpayers!

With amendments to legal precedents, this paradox could be resolved; however, there are others, whether due to the fact that legitimacy is denied to the other ‘de facto’ taxpayers, whether due to the fact that this legitimacy is denied as a general rule to ‘de jure’ taxpayers. We will return to those issues later in this paper. For now, suffice it to notice that, in summary, within the sphere of current STJ legal precedents with respect to ICMS, IPI and non-fixed ISS:

a) the so-called ‘de jure’ taxpayer cannot demand a repayment for a tax unjustly paid, unless he is able to prove he did not shift the burden to a third party, or that he is

\textsuperscript{31} STJ, 1st Panel, Special Appeal 1.278.668/RS and Special Appeal 1.299.303/SC.
authorized by third parties to receive it, and it is always presumed that shifts always and fully occur;

b) ‘de facto’ taxpayers cannot demand repayments on their own behalf either, because they are not parties to the legal relationship with the Tax Authority, except for the case of electricity consumers. Consumers, the so-called de facto taxpayers, are put in the most peculiar condition of being required to authorize de jure taxpayers to claim something they cannot claim on their own behalf.\textsuperscript{32}

5. Analyzing the Issue Within the European Community

5.1 Preliminary Considerations

Before initiating a comparative analysis, one must be mindful of possible singularities of legal orders to be compared, which should be taken into account when analyzing the solutions adopted in a particular place. For the purpose of this paper, the way prices are set and how taxes are levied upon them, as well as the position of buyers and sellers in the legal relationship under which undue payment takes place may differ from one country to another. This has obvious consequences in the use of passing-on defense, making it less acceptable depending on the case.

Therefore, the European Community was chosen for comparison purposes, where the issue came up regarding taxes similar to the Brazilian ICMS and IPI\textsuperscript{33}. The last section of this topic will briefly mention how the issue was addressed in other countries such as Canada, the United States, the United Kingdom, Israel and Australia; however, delving too deep into this subject would make this paper overly long. Therefore, the issue will be addressed at another time.

\textsuperscript{32} Therefore Ives Gandra da Silva Martins’s shrewd observation is still up to date; in his opinion, the notion of a de facto taxpayer, in addition to finding no support in Article 121 of the CTN, ‘is also a ‘neutered taxpayer’, since in theory he holds the right but cannot exercise it directly. It is worth noting, he would be a taxpayer that is able to block a repayment for an unduly paid tax, but not a taxpayer that is able to obtain a repayment.’ MARTINS, Ives Gandra da Silva. Repetição do Indébito. In: MARTINS, Ives Gandra da Silva (Editor). Repetição do Indébito. São Paulo: Resenha Tributária, 1983, p. 161. Indeed, there is absolutely no logic in preventing the Tax Authority from collecting the tax from a third party, and preventing this third party from obtaining a repayment when the tax was unduly paid, while ‘allowing’ the taxpayer to claim such restitution. As per NEVIANI, Tarcísio. A Restituição de Tributos Indevidos, seus problemas, suas incertezas. São Paulo: Resenha Tributária, 1983, p. 235.

\textsuperscript{33} Equivalent at least with respect to their influence on prices and to ‘shifting’ the corresponding burden onto final consumers of products or services encumbered by such duties.
5.2 How the Issue Emerged Domestically, in Danish Law

The *passing-on defense* initially appeared and was accepted by legal precedent in Europe within Danish Law, at the end of the first half of the twentieth century; coincidentally it was approximately at the same time that the Brazilian Supreme Federal Court became more strongly impressed by it. Nevertheless it is worth noting the singularity of Danish circumstances which led local judges to accept the tax authority argument: with the end of World War II, *grain prices were controlled* and the Government established a tax to be levied on transactions involving wheat. Grain traders protested against this charge and the government increased the maximum (controlled) price of the abovementioned grain in order to appease them. It was in this context that, after the tax’s illegal nature had been later acknowledged, traders claimed a repayment and the Tax Authority denied their request using the *passing-on defense*.\(^3\)

It should be noted that it was not the market that set the price of the merchandise that was sold and taxed, but the Government, which increased the controlled price with the specific aim of allowing traders to recover the tax burden. Controlled prices would not have been raised were it not for the tax whose repayment was under discussion. The government’s control over the economy, on the other hand, allowed the corresponding burden to be fully shifted.

This was the context in which the *passing on defense* was accepted by judges in that country, the same where the first case related to that subject appeared a few years later and was submitted to the analysis of the European Court of Justice (ECJ). This is worth knowing, for what often happens, above all when legal precedents are being analyzed, is that one does not pay attention to the context in which decisions are handed down. This will often lead to misrepresenting the *range* of the arguments accepted in such decisions.

5.3 Procedural Autonomy of Member States and the Hans Just case

The first case brought to the ECJ’s attention regarding the *passing on defense* also comes from Denmark, but it pertains to quite a different situation, of a strictly local nature,

in which the thesis was originally accepted by courts in that country, mentioned in the previous item. This was already an ‘expansion’ of an idea that appeared in a different context originally (and which made it less reproachable). This is the case known as *Hans Just v. Danish Ministry for Fiscal Affairs* (C-68/79), in which a beverage producer and importer questioned in court the levying of *excise tax* which imposed a heavier burden on products imported from other European Community member countries, singling them out in relation to Danish products, which violates EC community norms. Despite the fact that the duty was indeed considered undue, the Danish Tax Authority refused to repay the taxpayer, arguing that the corresponding burden had been shifted to beverage consumers; the local Courts were already familiar with this reasoning and accepted it.

Since this issue had repercussions on the application of Community Law, the issue was submitted to the ECJ, which regarded the Danish Tax Authority’s position as legitimate.

It should be noted, however, that the ECJ did not address the merits relating to the validity of the claim or whether it was correct to use the *passing on defense* in that case. What actually happened was the application of the *principle of autonomy*, because the court understood that although substantial law in this case is regulated communally, formal and procedural aspects should be addressed by domestic law (*procedural autonomy*). In other words, Community Law establishes how a duty may or may not be established and levied, but the process through which one who has unduly paid a duty will be restituted, active legitimacy to initiate it, applicable peremption and statutory limitation periods, interest rates, etc., those are all issues to be addressed by the Courts in each EC country, and the ECJ cannot interfere in such matters. This is the only reason why in this initial analysis, perhaps still not fully thought through in terms of the consequences of accepting the *passing on defense*, the ECJ tolerated such reasoning.

---

35 In general terms it is a tax similar to Brazil’s IPI (Tax on Manufactured Products).


37 In the same manner, see C-61/79, a judgment handed down a short time after the *Hans Just* case, in which the ECJ initially accepted the *passing-on defense* and recognized that paying a restitution does not constitute a subsidy or state aid to a taxpayer, forbidden within the community.
After that Tax Authorities in European Community Countries felt the ‘doors were open’ to using the abovementioned argument; throughout Europe the impediment that was until then mainly invoked by Denmark started being used more often. This was the case, for instance, in Italy, France and Austria.

5.4 The Beginning of Restrictions With the San Giorgio Case

The issue, however, is that the autonomy of procedural law is only relative and the separation between substantive and procedural law is not as clear as it may seem. The situation under review is notable proof of this, even more so because the discussion regarding legitimacy pertains to the ownership of the subjective (substantial) right itself to a repayment. On the other hand, even if it were not so, the relative nature of procedural autonomy comes from the circumstance that depending on how the procedure, as an instrument to enforce a substantive right, is regulated it may lead to the creation of traps or screens which aim at the opposite, that is, to consolidate and confer an appearance of legitimacy to flagrant illegalities. This is what the ECJ realized a short time later when it reviewed a case known as San Giorgio.

In a factual context that was similar to the Hans Just case, San Giorgio was a taxpayer who had paid a tax (a ‘sanitary tax’) in violation of Community Law, but whose repayment was denied by Italian authorities under the argument that the corresponding

---

38 The expression and its use to address the Hans Just case are credited to CAPRILLES, Theo. On why EU stand on the passing on defence equates to enriching the unjust. Available online at http://tup.tub.lu.se/tuur/download?func=downloadFile&recordOId=2006260&fileOId=2006296, access on 13/7/2012, p. 10.
39 By the way, there are practically no clear differences in real life, except between natural numbers and some other figures that exist in the abstract sphere only, and that are accessible through the human mind, such as geometric shapes. On this matter, see: DEEMTER, Kees Van. Not exactly: In praise of vagueness. Oxford: Oxford University Press, 2010, p. 9.
41 Case 199/82. Amministrazione delle Finanze dello Stato v SpA San Giorgio [1983] E.C.R. 3595, [1985] 2 C.M.L.R. 658. As Takis Tridimas notes (TRIDIMAS, Takis. The general principles of EU Law. 2.ed. Oxford University Press, Oxford, 2006, p. 438-439), the European Court of Justice adopted a non-interventionist position in the Hans Just case, and it was later forced to point out more explicit guidelines – undoubtedly limiting the use of passing on defense – in later cases. After repeating the precedent in which it accepted the passing on defense, ‘It stated, however that any requirement of proof which made virtually impossible or excessively difficult to obtain repayment was incompatible with Community law.’ (p. 439) Even before the notorious San Giorgio the ECJ was already giving signs that domestic autonomy, with respect to procedural aspects, interest rates, procedures, etc., allowed the passing-on defense to be invoked, but it could not be used to discriminate between national and foreign goods, and it could not make it difficult to apply community law. This position was confirmed, for example, in cases C-130/79 and C-826/79.
burden had been shifted to third parties and embedded in prices charged to consumers. However, when reviewing the matter the ECJ had a number of reservations or objections to the use of the passing on defense by the Tax Authority. Such reservations or objections practically correspond to rejecting the passing on defense or only accepting it in highly exceptional and duly justified cases (the first case regarding wheat producers in Denmark, mentioned in item 5.2 above, would perhaps be an example of this).

The ECJ's understanding at first was that one cannot presume that the duty unjustly paid by the taxpayer has been fully shifted to third parties by means of price setting. The burden may be only partially shifted, in which case a repayment could also be granted, albeit also in part only. Additionally, the crucial aspect is that there must be evidence that the burden has been shifted.

Although it is very difficult to prove that a tax burden has been shifted, it is even more difficult or impossible to prove it has never been shifted. Incidentally, the fact that an unduly paid tax has been shifted to a third party terminates or prevents a plaintiff from exercising his right to file a claim for a repayment; this fact, within the general theory of legal proof, is to be claimed (and substantiated) by the defendant. For all those reasons, even if the passing on defense were admissible, the burden of proof that shifting has occurred should fall on the Tax Authority, and the taxpayer cannot be compelled to provide evidence that the burden has not been shifted as a condition to file a claim for a repayment of the unduly paid tax.

The Court has also made it clear that even in cases where the Tax Authority has evidence of tax shifting, that in itself is no reason to deny a repayment to the taxpayer. This is because there may still be ‘harm’ to be remedied by means of a repayment, for even if the tax has been fully embedded into prices, it is undeniable that such an increase leads to falling sales.

---

42 That is why the ECJ considered in the previously mentioned San Giorgio case that ‘In a market economy based on freedom of competition, the question whether, and if so to what extent, a fiscal charge imposed on an importer has actually been passed on in subsequent transactions involves a degree of uncertainty for which the person obliged to pay a charge contrary to Community law cannot be systematically held responsible’. (§ 15)

43 This is what is expressly stated in the Brazilian Code of Civil Procedure (CPC), in Article 333, II. Tarcísio Neviani, incidentally, had already taken notice of this aspect, and very sharply so. On this matter, see: NEVIANI, Tarcísio. A Restituição de Tributos Indevidos, seus problemas, suas incertezas. São Paulo: Resenha Tributária, 1983, p. 150.

44 Among scholars who study this matter in Brazil, Tarcísio Neviani had already taken notice of this issue, highlighting that ‘the unduly paid tax simply reduces the taxpayer's profit, which ceases to realize it
price, had the market allowed, at greater profit; or he could have lowered his prices and increased sales, and also obtained greater profit. Therefore, as a rule, a tax repayment must be granted in any scenario in order to correct the damage caused by taxes unduly paid.

On the other hand, and this is the most important aspect of this issue, the ECJ found that, despite having the autonomy to legislate about procedural matters within domestic law, member countries cannot do so with the aim of making it extremely difficult or even impossible to obtain a restitution for a duty levied in violation of Community Law.

After that, when judging cases C-331/85; C-376/85; C-378/85 regarding the use of *passing-on defense* by the French Tax Authority, the Court even acknowledged that

> The Treaty establishing the European Economic Community must be interpreted as meaning that a Member State may not adopt provisions which make the repayment of charges levied contrary to Community law conditional upon the production of proof that those charges have not been passed on to the purchasers of the products that were subject to the charges and place the burden of adducing such negative proof entirely upon the natural or legal persons claiming repayment.

And in a way amending the premises that led it to accept the arguments in the *Hans Just* case, the Court clarified that this answer ‘does not depend on whether the national provision has retroactive effect, the nature of the charge at issue, or whether the market is free, regulated or monopolistic, either wholly or in part’.45

This understanding was later confirmed by the ECJ in several other occasions.46 When analyzing this issue regarding the *passing-on defense*, or even others relating to other aspects of repayment of undue taxes, the Court has always stressed the limits of that autonomy of domestic law with respect to formal or procedural aspects, as the effectiveness of Community Law.47

---


46 As per, e.g., C-30/2002; C-473/2000; C-441/98; C-442/98; C-104/86.

47 In its judgment of case C-386/87, for instance, the Court’s opinion was that a Member State may set an undelayable deadline for filing a claim for a repayment, as long as this deadline is not so short as to make the repayment itself impossible. At the time the Court believed that a deadline of three years would not make a repayment impossible to obtain. In case C-240/87, on the other hand, the Court regarded a change in how the...
5.5 The Unusual Case of Austria and the Actual Purpose of the ‘Passing-on Defense’

On that note, the case related to § 185 of the Vienna Tax Code (Wiener Abgabenordnung – WAO) is also worth mentioning. After a decision handed down by the European Court of Justice which considered an indirect tax established in Vienna (charge on beverages) to be invalid, that city’s local government introduced a provision in its Tax Code whose wording was very similar to that of Article 166 of the Brazilian CTN, with the clear aim of preventing taxpayers from obtaining restitutions, which they would certainly claim considering ECJ precedents. The same occurred in Brazil when Law 9.032/95 was enacted, which included in Article 89 of Law 8.212/91 a § 1.º ratifying the passing-on defense (as per item 4.3 above).

This WAO Article, which did not exist until March 2000, was introduced because Austrian Law states that declarations of unconstitutionality as a rule are only effective ex nunc. Therefore, if the tax had been declared unconstitutional by the Austrian Constitutional Court, it would not be repaid for the period prior to the declaration. Since the issue was not a violation of Austrian Constitution, but of Community Law, it was addressed by the ECJ, which refused to 'modulate’ the effects of its decision declaring the charge invalid. This was the context in which Vienna legislators came up with the ‘solution’ of § 185 of the WAO; this only makes it even more evident that the underlying notion in using the passing-on defense is not to repay the tax. It is honestly not about preventing a ‘de jure’ taxpayer’s unjustified enrichment, but simply creating the means for the tax, even when undue, no to be repaid, protecting the public treasury and preventing the enforcement of provisions whose violation caused the corresponding tax collection.

So, when analyzing the issue related to § 185 of the WAO in judgment C-147/01, the ECJ not only confirmed that the burden of proving ‘illegal enrichment’ should be taken on by the government and not the taxpayer (who could not be compelled to provide evidence of ‘non-shifting’), such as originally considered in the San Giorgio case, it also once again emphasized that shifting taxes on to prices did not necessarily correspond to a deadline to obtain restitution was determined as invalid; it was put into effect retroactively by France with the clear intention of preventing taxpayers from claiming that repayment.

lack of damages to be remedied by means of recovering undue payment, since ‘even if the charge has been fully embedded into set prices, the taxpayer may suffer damages associated with a decrease in sales (see appellate decisions Comateb and number 29 and Michaïlidis, number 35, already listed in the references).’

As for the circumstance that the article was a clear attempt to prevent the Court's understanding from being applied, which deemed the tax invalid, that same judgment noted that for legal certainty reasons, States may even establish limits for repayments (e.g. statutes of limitations), but these cannot be retroactive (such as § 185 of the WAO, which for this reason was considered contrary to the principle of protection of legitimate expectations). Furthermore, such limitations must respect the principle of effectiveness, ‘which determines that exercising the rights conferred by the community legal order will not become practically impossible or excessively difficult’; this sort of respect cannot be found in provisions that accept the thesis of the passing-on defense.

5.6 The Position of the De Facto Taxpayer

After it was established that the so-called ‘de jure’ taxpayer can legitimately claim a repayment for an unduly paid tax, and that the passing on defense, as a rule, cannot be invoked by the Tax Authority in order to make such a restitution extremely difficult or impossible, situations arose in which consumers, the so-called ‘de facto’ taxpayers, demanded restitutions; and when their claims were dismissed by local authorities they took them to the ECJ.

In those cases the Court ruled that, in principle, the final consumer, the ‘de facto’ taxpayer of the abovementioned indirect taxes, has no ad causam legitimacy to demand repayment. Or, more appropriately, the Court ruled that internal provisions of member countries which confer such legitimacy to ‘de jure’ taxpayers only do not violate Community Law. This is because although the final consumer economically bears the tax burden embedded in prices charged for merchandise and services at his disposal, there is no legal relationship between final consumer and Tax Authority.

49 C-147/2001, item 99.
50 C-147/2001, item 29.
51 C-147/2001, item 38.
In Case C-35/2005 (Reemtsma Cigarettefabriken Gmbh v. Ministero dele Finanze), for instance, a company hired a service provider who was a taxable person based in Italy; invoices for services provided included amounts charged for VAT (Value Added Tax) which were not in fact due. For this reason the company directly claimed a refund. The Italian Tax Authority, however, stated that a consumer has the right to be reimbursed for due VAT only, in cases where he leaves the corresponding country with taxed merchandise or services; he does not have the right to directly claim a refund or reimbursement for VAT unduly paid by the ‘de jure’ taxpayer, a seller.

The ECJ understood then that he, the so-called ‘de facto’ taxpayer and consumer, could not actually be reimbursed in the abovementioned situation, and that the service provider, a VAT taxpayer, had the legitimacy to claim a refund. Under the terms of item 33 in the judgment, ‘only the supplier must be considered to be liable for payment of VAT for the purposes of the tax authorities of the Member State where the services are supplied.’

Reinforcing the idea of procedural autonomy of Member States, the ECJ also emphasized that

in the absence of Community rules on applications for the repayment of taxes, it is for the domestic legal system of each Member State to lay down the conditions under which such applications may be made; those conditions must observe the principles of equivalence and effectiveness, that is to say, they must not be less favourable than those relating to similar claims founded on provisions of domestic law or framed so as to render virtually impossible the exercise of rights conferred by the Community legal order (see, inter alia, Case C-30/02 Recheio — Cash & Carry [2004] ECR I-6051, paragraph 17, and Case C-291/03 MyTravel [2005] ECR I-8477, paragraph 17).52

However, it is worth noting that the Court also emphasized that

the principles of neutrality, effectiveness and non-discrimination do not preclude national legislation, such as that at issue in the main proceedings, according to which only the supplier may seek reimbursement of the sums unduly paid as VAT to the tax authorities and the recipient of the services may bring a civil law action against that supplier for recovery of the sums paid but not due. However, where reimbursement of the VAT would become impossible or excessively difficult, the Member States must provide for the instruments necessary to enable that recipient to recover the unduly invoiced tax in order to respect the principle of effectiveness.53

As previously discussed, the Superior Court of Justice in Brazil has also been denying active ad causam legitimacy to final consumers, who are considered ‘de facto’

52 C-35/2005, item 37.
53 C-35/2005, item 42.
taxpayers of corresponding indirect duties. Like the ECJ, the Court's reasoning is based on the premise that there is no legal relationship between those consumers and the Tax Authority. That legitimacy is only recognized in special cases, such as that of electricity consumers, who are subject to tariffs. In addition, the way private utility companies provide their services puts the consumers in a position that is very close to that of a ‘de jure’ taxpayer, and not just consumer who is a ‘de facto’ taxpayer.

Nevertheless, this understanding - which was later ratified by the ECJ\(^5^4\) - cannot be compared with the opinion of the STJ after Special Appeal (Recurso Especial – RESp) 903.394/AL, according to which final consumers cannot demand repayment of ICMS or IPI levied on merchandise they have purchased. Judgments seem equivalent but they are not, since the legal precedents of both Courts must be seen in a broader and more global way. The ECJ denies legitimacy to de facto taxpayers as a rule, but it routinely recognizes the legitimacy of de jure taxpayers without the burden of proof of non-shifting. This makes significant difference, because it reveals how the ECJ is consistent while the STJ is the total opposite\(^5^5\). Furthermore, in cases where the de facto taxpayer’s illegitimacy could lead to a situation in which it is completely impossible to obtain a restitution, the ECJ admits this legitimacy in broader terms than the STJ, which makes exceptions for electricity consumers only.

Finally, the difference between the European VAT and Brazil’s ICMS and IPI must be discussed. In the case of VAT, invoices provided to consumers are much clearer and explicit, so much so that when tourists are returning home with merchandise bought in Europe they receive the corresponding refund at the airport, a privilege that is only granted in Brazil to de jure taxpayers who are exporters, and precariously so. This difference adds to the reasons why Brazil should adopt the understanding that, as a rule, repayments for unduly paid taxes, with respect to taxes usually regarded as indirect, should be granted to taxpayers legally defined as such; they should not be compelled to produce evidence that the tax’s economic burden has not been shifted and it is not initially relevant whether the duty’s burden has been shifted to the final consumer.

\(^5^5\) For an analysis of this incoherence – but still without references to the ECJ’s position or to European Law made in this paper - see: MACHADO SEGUNDO, Hugo de Brito. *Repetição do Tributo Indireto: incoerências e contradições*. São Paulo: Malheiros, 2011, passim.
In summary, within European Law and according to the understanding of the ECJ, restitutions for indirect taxes should be granted, as a rule, to taxpayers legally defined as such. The issue of finding out if the price charged on final consumers, the alleged ‘de facto’ taxpayers, is affected by whether the tax embedded in that price is invalid might be brought forward, but this is a matter that should be solved by taxpayer and consumer, in civil court if that be the case. This solution is very similar to the one proposed in Article 117 of the draft National Tax Code, devised by Gilberto de Ulhôa Canto, which unfortunately was never developed into law by relevant authorities. It reads as follows:

Article 117. The taxpayer of a tax obligation or the offender who has paid the penalty is a legitimate party who may claim repayment, even if the actual financial burden has been shifted to another person. Whoever provides evidence of shifting will have recourse against the reimbursed taxpayer or may become a party to the lawsuit as an assistant and request the judge to grant him restitution.

5.7. A Summary of the ECJ’s Opinion and Their Concerns

An analysis of STJ, STF and ECJ legal precedents on the issue of ‘indirect’ tax restitutions reveals that the latter is significantly concerned with how consistent the argument of ‘shifting’ the tax burden is (passing-on defense), and also with is implications on the effectiveness of rights violated by the institution and by levying undue taxes. In the ECJ’s opinion, this argument should not be used in any circumstances to make it impossible or extremely difficult for someone to exercise their right to a repayment.

In Brazil, an examination of STF and STJ legal precedents after 1940 reveals the complete opposite. Those Courts went to great lengths to create a thesis that makes it impossible, in a wonderfully incoherent way, for someone to exercise their right to a repayment for an unduly paid tax, whether they be a so-called ‘de jure’ taxpayer or a person who is mislabeled as ‘de facto taxpayer’. Perhaps the fact that the ECJ is further away from the influence of the Executive Branch of EC Member States can explain why this Court is more impartial and more concerned with the effectiveness of Community Law when some Member States rebel against it. The STJ and STF do not seem to share this concern with the effectiveness of the Constitution and of Laws, when it comes to tax issues.

In Brazil’s case one could say that there is Article 166 of the CTN, a rule which has supposedly led to legal precedents now being criticized. However, this criticism is
unfounded or it does not lead to the intended conclusion. First of all because the STF’s understanding regarding the passing-on defense precedes Article 166 of the CTN, and in a way it is responsible for that Article. Therefore, one cannot hold the article – or legislators, strictly speaking – accountable for the fact that legal precedents accept the thesis. Secondly, that article will be deemed unconstitutional if regarded as hindering access to Courts (judicial control), for its incompatibility with the provisions of Article 5.º, XXXV of the 1988 Federal Constitution is flagrant. Thirdly, because Article 166 of the CTN may be perfectly interpreted according to the Constitution, the understanding being that it does not apply indiscriminately to those taxes regarded as ‘indirect’, but strictly speaking only to those situations where the law places more than one person in the position of taxpayer in the tax relationship. In other words, Article 166 of the CTN is applicable only to the cases where there is more than one taxpayer legally defined as such, that is, more than one ‘de jure taxpayer’, or one ‘de jure taxpayer’ and one or more ‘tax-responsible persons’, under the terms of Article 128 of the CTN56, which is also accepted by the STJ, by the way.57

5.8. A Brief Account of How the Issue is Addressed in Other Countries

The passing-on defense can also be found in places such as Israel, Australia, United Kingdom, United States and Canada58. A detailed review of distinguishing features of those legal orders which may render the use of this argument more or less unjustifiable, as well as how it was received by Courts will be conducted at another time. For the time being it is worth mentioning only that the Supreme Court of Canada accepted this thesis


for some time, but has recently changed its legal precedents to reject it, rebuffing the idea that repayments granted to de jure taxpayers consist of unjust enrichment.

Among the arguments chosen by the Supreme Court of Canada is the fact that it is difficult to provide evidence of non-shifting, the consequences of this within the sphere of tax repayments, etc., such as outlined in ECJ legal precedents. In addition, it expressly stated that the notion of ‘unjust enrichment’ is *inapplicable* as grounds to granting or denying restitutions for unduly paid taxes. It reads as follows:

> “The passing-on defence is not available to the Crown in the context of a claim for the recovery of taxes paid pursuant to ultra vires legislation. The defence is inconsistent with the basic premise of restitution law. Restitutionary principles provide for restoration of what has been taken or received from the plaintiff without justification. Restitution law is not concerned by the possibility of the plaintiff obtaining a windfall because it is not founded on the concept of compensation for loss. The defence is also economically misconceived and creates serious difficulties of proof as there are inherent difficulties in a commercial marketplace of proving that the loss was not passed onto consumers.”

Indeed, if the tax is undue, the consequence of this must be reinstating *status quo ante*, by means of restitution. Whether this leads taxpayers to enrich unjustly is not to be investigated. This issue will be addressed again later.

6. A Few Observations About Solutions Provided

Based on all that has been discussed in this paper, and without even discussing the difficulty in classifying taxes as ‘direct’ or ‘indirect’ or the controversial issue relating to the analysis of ‘shifting’ the economic burden of a tax onto third parties, one may reach the conclusion that the treatment given to this issue by Brazilian legal precedents makes it extremely difficult or even impossible to obtain a restitution for a tax that has been unduly paid. Therefore, it becomes difficult or even impossible to reinstate the rights violated by the corresponding charge, and this goes against all constitutional norms that determine how taxes may be established and levied and how they cannot. The provisions of Article 5.º, XXXV of the 1988 Federal Constitution are even more emphatically violated, since taxpayers are refused the very access to the judicial control that will remedy the abovementioned violation.

---

Similar situations, when causing community provisions on how taxes may or may not be established and levied within the European Community to become ineffective, have led the European Court of Justice to impose countless limitations on the use of the passing-on defense by local Tax Authorities and Courts. Such limitations should be examined and reviewed by Federal Supreme Court and Superior Court of Justice Justices, from whom one expects a healthy change in legal precedents contained in STF Precedents 71 and 547. Article 166 of the CTN should be interpreted according to the Constitution, so that it is recognized that it is only applicable in cases where the law lists more than one taxpayer in the tax relationship, under the terms of Article 128 of the same Code.

Consequently, the legitimacy of ‘de jure’ taxpayers should be acknowledged so they may demand repayments for taxes unduly paid, even when regarded as ‘indirect’. The issue of possible repercussions of this matter on prices should be addressed in the civil sphere. This was already stated in Article 117 of the Code of Tax Procedure drafted by Gilberto de Ulhôa Canto. Therefore, if consumers of a particular product or service consider that the price they have paid is illegitimate, because the tax levied on it has been deemed undue, they may file a civil suit against the supplier. However, this should not prevent them from obtaining a repayment from the Tax Authority for amounts unduly paid.

Below is a summary of reasons that justify this opinion.

6.1. Shifting is Difficult to Determine

The first and main problem of using the passing-on defense and that calls for its abandonment is the fact that it is extremely difficult to determine whether a tax burden has been shifted. The analysis of the San Giorgio case confirms that this is not a question one can answer with ‘yes, shifting has occurred’ or ‘no, no shifting has occurred’. Shifting may occur in degrees. And what is worse, it may occur in multiple directions and orientations, and not only in the usually perceived route production → sales → final consumption. If the tax burden taken on by a seller increases, for instance, this may reflect ‘backwards’: its

---

suppliers may be forced to reduce their prices (shifting backwards) or even its employees may not get raises or they may be laid off.\textsuperscript{61}

Indeed, it is known that direct taxes may be shifted\textsuperscript{62} while indirect taxes may sometimes not be shifted. This buries once and for all the use of this classification to limit the right to a repayment for unduly paid taxes in relation to duties regarded as ‘indirect’.\textsuperscript{63}

In summary, there are countless factors that when combined lead to a trillion different scenarios, all of which should be taken into account when determining whether shifting has occurred, its direction, orientation and intensity. It is impossible for the Judiciary Branch to be aware of them all; also, as Neviani points out, it cannot hinder the problem in the worst way possible, by arbitrarily presuming shifting has occurred with respect to particular taxes and having the taxpayer undertake the impossible venture of refuting it.\textsuperscript{64} The best solution would be to just abandon the use of passing-on defense.\textsuperscript{65}

6.2. Even When Shifting Has Occurred, ‘De Jure’ Taxpayers Experience ‘Harm’ that Should Be Remedied

Another aspect that should be taken into account when rejecting a Tax Authority’s use of the passing-on defense in claims for repayment of taxes unduly paid is that even if the tax has been shifted to third parties, the taxpayer’s right to a restitution must prevail if the payment was undue.

\begin{itemize}
  \item CAPRILLES, Theo. On why EU stand on the passing on defence equates to enriching the unjust. Available online at \url{http://lup.lub.lu.se/luur/download?func=downloadFile&recordOId=2006260&fileOId=2006296}, access on 13/7/2012, p. 24.
\end{itemize}
One must reject the argument of ‘unjust enrichment’ introduced in the judgment handed down by the abovementioned Supreme Court of Canada and by most Brazilian jurists. Additionally, Tarcísio Neviani and the European Court of Justice, in the San Giorgio judgment, also sensibly noticed the fact that making the taxpayer's products unjustly more expensive leads to a fall in sales and therefore causes ‘harm’ that should be remedied by granting a restitution for unduly paid taxes, regardless of whether the tax burden has been shifted or not.

6.3. Distinguishing Between Tax and Price

The most relevant aspect in this entire discussion, though, may be the fact that the tax paid by the ‘de jure’ taxpayer should not be confused with the price paid by the ‘de facto’ taxpayer, even if the tax is fully ‘embedded’ into the price. Their legal grounds are different, and the fact that the first is undue does not make the second undue as well.

In fact, taxes, together with other costs and a profit margin (which is not controlled and may be higher, lower or even non-existing in some situations), are factors that must be taken into account by sellers when setting their price. This price, however, is not defined by those costs alone, but by several other market factors. And since profit is not controlled, one can say that a lower tax burden would cause the seller to obtain greater legitimate profits, if the market allowed him to sell his products for the same price.67

---

In summary, in addition to all that has been presented in previous items, shifting of indirect taxes, when it occurs, makes the final consumer pay a higher price and that is all. However, the amount paid by the consumer, the so-called ‘de facto’ taxpayer, is not a tax. It is a price, and it does not cease to be so because the seller pays taxes and takes them into account when setting his prices. Price does not become unjustified either if one of the components taken into account when they are being set is deemed invalid.

If a seller sets his price bearing in mind his obligation to pay expensive rent, and if the buyer accepts paying this price and purchases the merchandise, thereby entering into a sales contract, the fact that he later finds out that the rent is not so expensive after all does not make the price already paid undue, on its own. The price is due, because it was validly agreed upon, and little does it matter which factors led the seller to set it at the amount accepted by the buyer. This acceptance is indeed relevant. And just as rent, wages and other costs are taken into account, so are taxes, whether they are direct or indirect.

6.4. Notion of ‘Unjust Enrichment’ is Inappropriate, in This Case

70 ‘... when the taxpayer subject to the tax obligation incorporates the amount due for the tax into his operational costs, said tax ceases to be a duty, which is ontologically extinguished with its payment to the treasury and becomes only a cost that is to be eventually covered by the price paid by the persons who purchase the goods or services’. NEVIANI, Tarcísio. A Restituição de Tributos Indevidos, seus problemas, suas incertezas. São Paulo: Resenha Tributária, 1983, p. 122.
It is precisely because taxes and prices are different that when sellers raise their prices to make up for the tax’s (economic) burden, the amount paid as price is legitimate even if the tax is later considered undue. Therefore, there is no reason to state that the seller has not taken on a ‘burden’ with the payment of the undue tax, and if he is granted a repayment it will not consist of unjust enrichment.

The unjust enrichment argument is also rejected when one considers that without the (undue) tax the seller could have charged the same price for the product and obtained greater profit. Therefore, even when the tax is shifted to the consumer by increasing prices, legally speaking the undue tax causes the seller to either lose part of his profit, because of the price he charged, or it causes a fall in sales because the price charged could have been lower. In any case, levying the tax causes ‘harm’ that is subject to remedy, despite alleged and full shifting.

As if this were not enough, if the tax is unjustified, one must grant a repayment as a way of redressing the violated legal order\(^\text{71}\). The thing which gives rise to the duty of repayment is not a taxpayer’s ‘impoverishment’, but rather violation of the law, which must be redressed without an investigation on who becomes richer or poorer as a result of this. This is what the Supreme Court of Canada realized, and very appropriately so\(^\text{72}\).

6.5. The Burden of Proof of Shifting or of Unjustified Enrichment

Despite all that has been said above, if one could consider an extremely exceptional situation where the thesis of shifting the tax burden and unjust enrichment might be somehow relevant, the burden of proof should actually always fall on the Tax Authority, a defendant who would therefore be opposing a fact that blocks or changes the plaintiff’s right to repayment of unduly paid taxes.

In fact, as a rule the right thing to do is to reject the passing-on defense. However, if its use could be justified in an extremely specific case, the burden of such proof and of

\(^{71}\) As Theo Caprilles points out, “it seems inconsistent to apply the unjust enrichment doctrine, which as its language indicates derives its legitimacy from justice, in favor of a State that contravene the law in a dispute with an innocent party.” CAPRILLES, Theo. On why EU stand on the passing on defence equates to enriching the unjust. Available online at http://lup.lub.lu.se/luur/download?func=downloadFile&recordOId=2006260&fileOId=2006296, access on 13/7/2012, p. 25

presenting the facts that justify its use cannot fall on anyone other than the Tax Authority claiming it.

6.6. It Is Impossible to Recognize the Rights of Someone Who Is Not a Party to the Legal Relationship

Another aspect that should be taken into account in order to finally reject the passing-on defense within the sphere of tax restitutions for unduly paid charges is that it is incoherent to consider someone as a party to the legal relationship who by definition is not.

One cannot deny legitimacy to the ‘de jure’ taxpayer by claiming a tax has been shifted and not acknowledge the legitimacy of the ‘de facto’ taxpayer, who was the alleged target of that shifting. If one cannot be repaid because the duty was ‘actually’ paid up by another, the latter should have their right to repayment recognized.

And yet granting legal relevance to the ‘de facto’ taxpayer and awarding him rights that are typical of those who are in the position of taxpayers in the tax legal relationship contradicts the very definition of their position as being merely ‘de facto’.

In addition to this incoherence, there are other difficulties. How is he, a de facto taxpayer, to demand repayment of a tax that has only been shifted to the price he paid, will he have to prove that the ‘de jure’ taxpayer has indeed paid the duty? It should be noted that the tax may have been taken into account when the price was set; it may have been ‘economically’ borne by the final consumer; but it might not have been paid by the de jure taxpayer to the public treasury. Should the tax authority be compelled to repay that which they have not received? Will the de facto taxpayer have to prove that the de jure taxpayer has indeed paid the duty? How?

Such complicating factors only show the utter lack of logic in considering someone who by definition is not a party to any legal relationship as a holder of ‘rights’, when they take on the burden economically only, or ‘de facto’. And it is also illogical to deny those rights to a person who is a party to this relationship as a taxpayer, having thus been considered by the legislation which created the tax.

6.7. What Are Possible Legal Effects of a Tax’s ‘Indirect’ Nature?
Considering what has been discussed in the previous items, one could question whether it is in any way useful to classify taxes as direct and indirect, as well as considering the shifting phenomenon.

Actually, the fact that a duty indirectly encumbers the taxpaying ability revealed by a person other than that defined by the law as a taxpayer, and the possibility that the economic burden of this tax could be shifted to those persons by an increase in prices charged for goods and services they consume, however difficult to determine, may be regarded by legislators in a macro\textsuperscript{73} scenario when defining tax policies and determining the tax rates of corresponding duties. This explains why the classification remains\textsuperscript{74}, because the problem is not the classification itself but rather the legal effects that may or may not be obtained from it.

Therefore, if one knows that the tax tends to increase prices, like any other cost, this may be taken into account when setting the corresponding tax rates, according to the goods. This is what the 1988 Federal Constitution provides, with respect to ICMS and IPI, which are selective according to how essential the encumbered merchandise is. It can also determine the creation of devices aimed at preventing those taxations from suspending the duty’s neutrality; in order to do so, the non-cumulative (value added) system should be introduced.

It should be noted, however, that selectivity as well as non-cumulativity (value added technique), within the tax sphere, are both consequences of the notion that so-called indirect taxes increase the price charged for goods and services on which they are levied, but the legal nature of the amount paid by consumers of such goods and services is still that of a price and it is not affected if the duty which makes it more expensive is later considered undue.\textsuperscript{75}

7. Conclusions

\textsuperscript{75} MACHADO SEGUNDO, Hugo de Brito. Repetição do Tributo Indireto: incoerências e contradições. São Paulo: Malheiros, 2011, items 7.28 to 7.33 and 10.35.
Considering what has been discussed throughout this paper, the conclusion, in summary, is that:

a) the classification of taxes as direct and indirect may be employed for didactic purposes, to determine the tax rate of duties, to guide decisions pertaining to tax policy, but not to deny a taxpayer defined as such the rights inherent to his condition, above all when this occurs while those same rights are not granted to a third party on to whom the tax burden has supposedly been shifted;

b) one can only consider applying Article 166 of the CTN in those situations where legislation lists more than one taxpayer, under the terms of Article 128 of the CTN. In such cases the legal relationship may be questioned by any of them, jointly or severally, prior to payment (e.g. by means of an action for annulment, a writ of mandamus, etc.). Applying the abovementioned article should only be considered when the issue pertains to a claim that aims to obtain repayment for sums unduly paid by a taxpayer or tax-responsible person, in which case a restitution will be granted to the person who can prove that he complied (legally and not economically) with the tax.

References.


PARLAK, Süleyman. Passing-on Defence and Indirect Purchaser Standing: Should the Passing-on Defence Be Rejected Now the Indirect Purchaser Has Standing

PIGNATELLI, José Miguel Martínez-Carrasco. "La devolución de lo indebido tributario en el derecho de la Comunidad Europea". Available online at http://ddd.uab.es/record/38056?ln=ca.


