

# *Tax Litigation Newsletter*

*Issue 2  
August 2011*



## *Fighting City Hall ... and winning*



**Rob Shantz**

Legal Partner

*Welcome to the PwC Tax Litigation Newsletter, Issue No. 2.*

*It is sometimes said that " ... you can't fight City Hall." Of course, this refers to how difficult it can be to make a government authority change its view. There is sometimes the perception that this is particularly true in Ukraine, and that the authorities are capable of being especially unaccountable and unresponsive to other points of view. With this in mind, I'm happy to share that a high percentage of the tax litigation cases which we have been involved with have received fair rulings on the merits, which generally results in positive outcomes for our clients.*

*Of course, litigation everywhere suggests risks. Before deciding to proceed, it is important to weigh the implications of not challenging an assessment against factors such as the time and cost of litigation, the likelihood of success, and, in some cases, the likelihood of a judgement being satisfied even if successful. (And, unfortunately, in broader commercial litigation there is sometimes an additional concern that the other party may attempt to unduly influence the proceedings.) While this analysis should be conducted on a case by case basis, our experience is that, in the right circumstances, litigation is a very viable option to address disputes with the tax authorities. In other words, you can fight City Hall ... and win.*

*PwC can provide all of the necessary support for tax litigation proceedings, such as:*

- Support before and during tax and customs audits;*
- Technical analysis;*
- Communication with the authorities;*
- Administrative appeals; and*
- Representation in court proceedings.*

*And last but not the least, PwC Ukraine will be soon hosting its 2nd annual conference on tax litigation. This conference will take place on 5 September 2011 at the Opera Hotel in Kyiv. We will be sending invitations shortly, and encourage anyone who would like to attend but does not receive an invitation to contact us and we will do our best to accommodate all such requests.*

## **VAT Refund**

The Highest Administrative Court of Ukraine (the Court) in its Ruling of 6 October 2010 confirmed that a taxpayer is entitled to a VAT refund irrespective of the results of the tax audits of its business counterparties / suppliers.

### **Facts**

A taxpayer filed a claim to recover a VAT refund from the state.

The tax authorities objected to the taxpayer's claim, asserting that the tax audits of this taxpayer's counterparties were not performed. No other grounds for refusing the VAT refund were stated.

The Court ruled that the law does not set forth a requirement that a taxpayer's right to a VAT refund is dependent upon the results of the tax audits of its counterparties in the chain of supply.

The Court pointed out that certain findings could be considered as grounds for refusal of a VAT refund, namely:

- Relations between the parties were intended for the unlawful obtaining of tax benefits;
- The taxpayer was aware of the unlawful actions of its supplier; or
- The taxpayer assisted a supplier in evading tax obligations.

None of the above-mentioned facts were determined in the court proceedings. Thus, the Court ruled in favour of the taxpayer.

### **Consideration**

It is advisable to consider developing contractor / supplier acceptance procedures to build a stronger defence file. Also, it is advisable to collect all relevant evidence confirming the bona fide character of a counterparty's activity.

*(Ruling of the Highest Administrative Court of Ukraine of 06 October 2010, case No. 2-a-12462/08/0570)*

## **Sham Transactions**

In many instances the tax authorities deny the right of taxpayers for VAT credit based on the fact that tax invoices are signed by an unascertained person. A recent court judgment implied that this fact should not be taken into consideration if the actuality of a business transaction is proved.

### **Facts**

A taxpayer filed a claim for cancellation of a tax assessment issued as a result of a tax audit. During the tax audit the tax authorities revealed that tax invoices, based on which the taxpayer claimed VAT credit, were signed by an unascertained person. Based on the results of the tax audit, the tax authorities issued tax assessments. The taxpayer challenged them in court.

The Highest Administrative Court of Ukraine ruled in favour of the taxpayer. The case was then brought to the Supreme Court of Ukraine (the Court) by the tax authorities. The Supreme Court of Ukraine supported the tax authorities and remanded the case to the court of the first instance.

Although this case was not favourable for the taxpayer, the Court stipulated that a tax invoice, signed by an unascertained person, cannot be a ground for claiming VAT credit, if there are other facts / evidence proving the transaction did not actually take place.

### **Consideration**

While adverse to the taxpayer in this particular instance, it might be argued that this judgment of the Court indicates that, if evidence of the actuality of transactions is available, the taxpayer should be entitled to VAT credit even if tax invoices were issued by an unascertained person. Clearly, taxpayers should collect as much evidence as possible for proving the actual occurrence of their business transactions.

*(Ruling of the Supreme Court of Ukraine as of 21 January 2011, case No. 21-37a10)*

## **Determination of the Actual Occurrence of Business Transactions**

The Highest Administrative Court of Ukraine (the Court) issued a letter that provides further clarifications to courts of lower instances on the determination of sham transactions.

In particular, the Court stated that relevant documents should be taken into account only if it is established that the transactions actually took place. To determine if transactions took place, the Court suggested considering, among others, the following factors:

- Transfer of assets / services in the course of the transactions, i.e. if all documents pertaining to the transactions are in place; if the taxpayer's counterparty had sufficient assets / resources to execute its obligations, etc;
- Tax status of the parties to the transaction, i.e., if they were properly registered as VAT / tax payers in the course of execution of the transaction; if a taxpayer was aware of defects (violations) in the actions of its counterparty, etc;
- Relationship between the transaction and business activity of the taxpayer. Importantly, to meet this criterion, it is sufficient to determine that a taxpayer had a business purpose to use purchased goods / services irrespective of the actual results of such use.

The Court suggested considering these factors in their entirety before making a decision, i.e., if a single factor is not fully met, it should not necessarily lead to negative tax consequences for the taxpayer.

### **Consideration**

It appears that this letter of the Court continues the series of letters aimed at clarifying how and when sham transactions may be determined. However, several important issues are still not covered, e.g., the Court did not confirm that the tax authorities are not empowered to declare agreements as void (even though technically the tax office does not have such authority).

*(Letter of the Highest Administrative Court of Ukraine No. 742/11/13-11 of 02 June 2011)*

## **Limitation Period**

The Highest Administrative Court of Ukraine (the Court) issued a letter clarifying the limitation period to challenge tax assessments.

The Court clarified that:

- Tax assessments issued in the period from 30 July 2010 – 01 January 2011 may be challenged within one month as stipulated by part 5 Article 99 of the Code of Administrative Proceedings of Ukraine;
- Tax assessments in the period after 01 January 2011 (after the Tax Code entered into force) may be challenged within 1,095 days as stipulated by paragraph 56.18 of the Tax Code.

It is worth mentioning that, in fact, during the period 30 July 2010 – 01 January 2011 the approach of the lower administrative courts in respect of applying the limitation period was inconsistent. While some courts applied the mentioned one-month term, others tended to continue using a 1095 day period.

### **Consideration**

It appears that this letter of the Court is rather positive, as inconsistencies between the procedural provisions of the Tax Code and the administrative procedural legislation are clarified.

*(Letter of the Highest Administrative Court of Ukraine as of 05 July 2011 No. 945/11/13-11)*

## ***Contacts***



***Ron Barden***

Partner, TLS practice leader  
ron.j.barden@ua.pwc.com



***Rob Shantz***

Legal Partner  
rob.shantz@ua.pwc.com



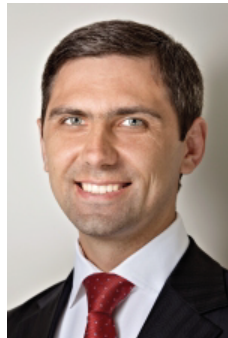
***Slava Vlasov***

Tax Partner  
slava.vlasov@ua.pwc.com



***Igor Dankov***

Senior Manager  
igor.dankov@ua.pwc.com



***Andrey Pronchenko***

Senior Attorney  
andrey.pronchenko@ua.pwc.com



***Serhiy Verlanov***

Attorney  
serhiy.verlanov@ua.pwc.com

This publication has been prepared for general guidance on matters of interest only, and does not constitute professional advice. You should not act upon the information contained in this publication without obtaining specific professional advice. No representation or warranty (express or implied) is given as to the accuracy or completeness of the information contained in this publication, and, to the extent permitted by law, PricewaterhouseCoopers LLC, its members, employees and agents do not accept or assume any liability, responsibility or duty of care for any consequences of you or anyone else acting, or refraining to act, in reliance on the information contained in this publication or for any decision based on it.

© 2011 Limited liability company «PricewaterhouseCoopers». All rights reserved. In this document «PwC» refers to Limited liability company «PricewaterhouseCoopers», which is member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.