

Tax Litigation Newsletter

*Issue 5
February 2013*



In this Issue of the Tax Litigation Newsletter, we focus on the recent practice of the Highest Administrative Court of Ukraine (the HACU) in cases related to challenging tax notification decisions. We selected those cases that we consider interesting from the practical implementation perspective.

***Transactions
alleged to lack
substance (sham
transactions):
current practice
of the HACU***

The tax authorities lost the case regarding the annulment of a contract as a sham transaction (the decision of the HACU dated 17 September 2012 in the case № K-45178/09).

Facts

The tax authorities filed a claim on the annulment of the contract between the Company and its counter-party. The principal evidence asserted by the tax authorities was the explanation of the counter-party's director that he had not signed the contract and he had not had any relations with the Company.

The court of the first instance and the court of appeals rejected the demands of the tax authorities' claim.

The tax authorities submitted a cassation claim.

The HACU partially satisfied the tax authorities' cassation claim.

Position

The HACU stated in its decision that the contract cannot be annulled as a sham transaction due to the explanation of one party's director if there is evidence of its fulfilment according to the valid legislation. Moreover, the HACU stressed that the annulment of a contract as concluded with a purpose which was contrary to the state and public interests, cannot be the subject of an administrative claim.

Consideration

Taking into account the HACU's decision, the tax authorities will likely maintain their practice of declaring the annulment of contracts in tax audit reports without challenging the contract's validity in court.

Nonpayment of taxes by a counter-party cannot be a ground for challenging a company's right for VAT tax credit

In the decision dated 31 October, 2012, in the case № K/9991/74364/11, the HACU one more time followed the principle of individualization of liability – i.e., a bona fide taxpayer cannot be liable for the inappropriate actions of its counter-parties.

Facts

The tax authorities challenged the right of the Company for VAT tax credit because the counter-party of the Company had not paid the VAT and the state budget had not received the VAT regarding these relationships.

The Company challenged the tax assessment in court. The court of the first instance and the court of appeals satisfied the Company's claim, both considering the contract to have been properly concluded and executed. Sufficient evidence was submitted to the court to support the position of the Company, including acceptance acts, invoices, payment orders, and tax invoices .

The HACU affirmed the decisions of the lower court instances.

Position

The HACU ruled that the Company cannot be responsible for nonpayment of the taxes by its counter-party if there is no evidence confirming an agreement between the Company and his counter-party to achieve an illegal tax benefit.

Being a bona fide taxpayer, the Company is not obliged or empowered to control timely payment of taxes by its counter-parties.

Consideration

The HACU confirmed that the tax authorities should not challenge the taxpayer's right for VAT tax credit due to nonpayment of taxes by their counter-party. This principle is not applicable if there is evidence confirming agreement between the taxpayer and their counter-party to achieve an illegal tax benefit.

Economic discretion in business activity

The HACU's decision dated 17 October, 2012, in the case N^o K/9991/41983/12, confirmed that the taxpayer's right to VAT tax credit, proved with the proper documents, cannot depend on the economic expediency of the transaction.

Facts

As a result of a tax audit, the tax authorities challenged the right of the Company for VAT tax credit due to the alleged absence of economic rationale for the transaction, and obliged the Company to pay additional VAT to the budget.

The Company challenged the tax assessment in court. The court of the first instance satisfied the claim, but the court of appeals cancelled the decision of the court of the first instance. The HACU overruled the decision of the court of appeals and confirmed the right of the Company for VAT tax credit.

Position

The HACU canceled the decision of the court of appeals on the basis that the taxpayer's right to VAT tax credit should be assessed in regard to the evidence confirming an intention of the taxpayer to obtain economic benefits as a result of the transaction.

The HACU stated in its decision that neither tax nor judicial authorities have the right to check the economic expediency of the taxpayer's business decisions.

Consideration

The practice of the HACU confirmed a company's right to economic discretion in their business activity and strengthened the taxpayer's position in similar disputes.

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



Andrey Pronchenko

Senior Manager
andrey.pronchenko@ua.pwc.com



Serhiy Verlanov

Legal Manager
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.

©2013 Limited liability company «PricewaterhouseCoopers». All rights reserved.

PwC refers to the Ukrainian member firm, and may sometimes refer to the PwC network. Each member firm is a separate legal entity. Please see www.pwc.com/structure for further details.