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LT in Focus
Issue 3
May 2016 – September 2016

LT in Focus

Review of Interesting Court Cases

Court Practice

In this 3rd issue we will be looking at some of the most interesting and important court cases between May and September 2016:

Taxation

- Understatement of the value of coal exports
- Accrual of CIT at the source of payment due to the lack of an apostille on certificates of residency issued by the Financial and Tax Authority of the Russian Federation
- Offset of VAT on adjusted invoices

Customs disputes

- Change to the EEU FEC CN

Contractual Issues

- Recovery of payments for the use of railway wagons in the absence of an agreement between parties

Understatement of the value of coal exports

Ruling of the Supreme Court (hereinafter – "the Supreme Court of RK") Judicial Board for Civil and Administrative Cases dated 11 May 2016 on case 3гп-327-16

Bogatyr Komir LLP

Decision amending a previous court ruling

In accordance with the results of a comprehensive tax audit of "Bogatyr Komir" LLP (hereinafter – "the Taxpayer") for the period between 1 January 2009 and 31 December 2012 resulted in the accrual of additional income due to the use of an unjustified trader margin on coal exported for further resale in Russia.

The Taxpayer filed a claim to have the tax authorities' actions recognised as unlawful and the results of the audit annulled.

Case history

Period	Instance	Result
October 2015	Pavlodar Oblast Specialised Inter-Regional Economic Court	The Taxpayer demands upheld in part
June 2015	Appeal Judicial Board for Civil and Administrative Cases of the Pavlodar Oblast Court	Court ruling of the previous instance left unchanged
May 2016	Supreme Court	Rulings of the previous instances upholding the Taxpayer demands annulled. The remainder of the court rulings in question remained unchanged

Supreme Court position:

Supreme Court sessions established that the Taxpayer had used trader margins calculated by an independent consultant based on the Ruslana - Bureau van Dijk database.

According to the tax authorities, the margin used is unjustifiably high, as the values used differ from findings from research carried out at the tax authorities' request by Bureau van Dijk Electronic Publishing S.A.

The Bureau van Dijk Electronic Publishing S.A. findings are also based on the Ruslana - Bureau van Dijk database.

At the same time, the tax authorities establish the following reasons for the overstatement:

- the final sample of traders compiled by the independent consultant to determine the market value of the margin included Russian companies that do not meet sampling criteria for comparable companies
- the Taxpayer set the margin using gross profit data which includes profit from both core and auxiliary activities, which was included in the comparable traders sample
- during the audit, Bogatyr Komir failed to provide the tax authorities with economic justification for the margin, in accordance with subpoint 5) of point 3 of article 5 of Law №67-IV dated 5 July 2008 *On Transfer Pricing*

Based on the above, the Supreme Court of RK ruled that no additional evidence was required and that the circumstances of the case had been well established.

For this reason, the Supreme Court of RK established a significant violation of material and procedural law by the local court and ruled that (i) the court acts upholding the Taxpayer demands be annulled (ii) a new ruling be issued rejecting the application to recognise tax audit findings as unlawful and annulling the same.

Thus, the Supreme Court of RK took the tax authorities' position and did not uphold the Taxpayer's claim.

Source: *Court case reference guide of the integrated information and analytical system of judicial authorities of the Republic of Kazakhstan*

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Accrual of CIT at the source of payment due to the lack of an apostille on residency certificates issued by the Financial and Tax Authority of the Russian Federation

Resolution of the Astana Judicial Board for Civil Cases of the Supreme Court dated 27 July 2016 on case 2a-3989-16

Joint Stock Company Centrekazenergomontazh

Decision on the rejection of the company's claims

On 21 December 2012, Centrekazenergomontazh (the "Company") entered into contracts with two Russian-resident companies, under which the latter was responsible for the work to be performed. The work performed was duly confirmed by the Company providing a court with the relevant acts of completion.

Tax audit № 4 from 4 April 2016 established that the Company should have withheld corporate income tax ("CIT") at the source on non-resident legal entities from the above parties. The Company went to court to request that the State Revenue Committee recognise the section of the tax audit notification covering CIT at the source of KZT 7,683,642 and late payment interest of KZT 2,752,777 as invalid, stating that the tax authorities had acted incorrectly, citing a violation of point 1 of article 193 and point 6 of article 212 of the Tax Code. The Company took the position that because of articles 193, 212 and 219 of the Tax Code and in accordance with a treaty between Kazakhstan and Russia, to avoid double taxation and in connection with the provision of supporting residency documents, it did not withhold CIT on the above counterparties. In its lawsuit, the Company confirmed that it had provided copies of Russian residency certificates for its counterparties and cover letters to the regional tax authorities. However, the State Revenue Committee refused to take the documents in question into consideration.

The court of first instance did not uphold the Company's claim against the State Revenue Committee. In its appeal, the Company asserted that the court had interpreted the Tax Code incorrectly and asked that the court ruling be annulled and a new ruling be issued upholding its claim.

The court case established the following:

- the court of first instance's conclusion about the legality of the tax agent's requirement to file notarised copies of counterparty residency certificates with the local state revenue authorities according to points 4 and 5 of article 219 of the Tax Code was recognised by the judicial board as justified and corresponding to the case. According to point 5 of article 219 of the Tax Code, the document in question should have been notarised in Russia. Likewise, the signature and stamp of the body certifying a document supporting a non-resident's residency and the signature and stamp of a foreign notary if a copy of a document is notarised should be legalised in accordance with the procedure established by Kazakhstan law.
- the court of first instance ruling that *unnotarised and unapostilled copies of residency certificates of the abovementioned counterparties* referred to above may not be filed with a court as proof of the compliance with the requirements expressed in article 212 of the Tax Code was recognised as justified.

Case history

Period	Level	Outcome
June 2016	Court of First Instance	Lawsuit rejected
July 2016	Court of Appeal	Ruling of the Court of First Instance left unchanged

Position of the Astana City Court Judicial Board for Civil Cases

The Astana city court concluded that the Company did not provide the State Revenue Committee with trustworthy evidence in the form of a duly executed certificate for the purposes of complying with the requirements of tax legislation on the avoidance of double taxation.

Source: *Court case reference guide of the integrated information and analytical system of judicial authorities of the Republic of Kazakhstan*

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Offset of VAT on adjusted invoices

Kyzylorda Oblast Court Judicial Board Ruling dated 8 June 2016 on case 4399-16-00-2a/349

Joint Stock Company Turgai Petroleum

Decision on the rejection of the Company's claims

The targeted tax audit of Turgai Petroleum JSC (hereinafter – "the Taxpayer") for activities between 1 October 2011 and 31 December 2012 resulted in expenses for goods purchased, services provided and work performed being removed from taxable turnover and offsettable VAT being reduced. Among others, the VAT on adjusted invoices were withdrawn from the offset.

The Taxpayer went to court to have the notification and act of documentary tax audit recognised as illegal and annulled.

Cash history

Period	Level	Outcome
March 2016	Court of First Instance	Company lawsuit rejected
June 2016	Court of Appeal	Court of First Instance ruling left unchanged

Position of the Astana City Court Judicial Board for Civil Cases

The court established that the Taxpayer had failed to observe the requirements for drafting invoices according to point 5 of article 263 of the Tax Code, which is treated as grounds for removing VAT in invoices that do not meet Tax Code requirements.

According to subpoint 3) of point 1 of article 257 of the Tax Code, VAT is not offset and recorded in accordance with the procedure established by point 12 of article 100 of the Tax Code, if it is due following the receipt of goods, work and services for which invoices were issued that do not meet Tax Code requirements. None of the adjusted invoices as at 18 November 2015 meet the provisions of point 14 of article 263 of the Tax Code, whereat, according to the court, the tax authorities were justified in withdrawing VAT from the offset.

Source: *Court case reference guide of the integrated information and analytical system of judicial authorities of the Republic of Kazakhstan*

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Change to the EEU FEA CN commodity classifier

Ruling of the Atyrau Oblast Court Judicial Board for Civil Cases dated 31 May 2016 on Case 2399-16-00-2a/472

Consolidated Supply and Services International LLP

Decision on the rejection of the company's claims

In 2014, "Consolidated Supply and Services International" LLP (the "Company") imported four 8.5 m speed boats made by Marine Frontiers PVT LTD. To declare the boats, the Company entered Eurasian Economic Union Foreign Economic Activity Commodity Code ("EEU FEA CN") 8901 90 900 0 – Other Floating Freight and Freight-Passenger Vehicles. The import customs duty rate for the code in question is 5% of the customs value of the goods.

After an in-house audit, the customs authorities issued an audit act, notification to eliminate violations and a decision to classify goods under EEU FEA CN 8903 92 100 0. Import customs duties for the new code are 15% of the customs value of goods. Consequently, the customs authorities also issued notification to pay overdue customs payments, taxes and late payment interest of KZT 48,249,552.

The Company went to court to annul the customs authorities' demand to pay customs duties, taxes and late payment interest as it did not agree with the reclassification of the goods.

Supreme Court sessions established:

- the EEU FEA CN position 8901 is used for cruisers, tourist boats, ferries, freight ships, barges and similar floating vessels transporting passengers or freight: 890190 – freight and freight-passenger floating vessels and others. It includes all floating vessels used to transport passengers or freight, apart from those included in position 8903 and life vessels (apart from rowing boats), military vessels and sanitary vessels (position 8906); any such vessels may be marine or inland water vessels (for example, lakes, canals, rivers or river deltas).
- the EEU FEA CN position 8903 belongs to yachts and other floating vessels used for leisure or sport; rowing boats and canoes (+): 890392 – motor boats and speed boats, apart from boats with outboard motors. It includes all floating vessels for leisure or sport and all rowing boats and canoes; yachts, vessels with water-jet engines and other sail boats and motor boats, dinghies, canoes, boats with sculling oars, sculls, pedalos, sport's fishing boats, inflatable vessels and boats that may be packed or dismantled.
- the Company has a certificate from Lloyd's Register EMEA stating that imported goods are speedboats and rapid response vessels with diesel engines and water-jet propulsion.
- the Lloyd's Register EMEA certificate refers to a DNV-GL certificate issued to Marine Frontiers PVT.
- according to advice from Khabibullina H.Y., an expert in the field, the DNV-GL certificate is issued by the classifiying society that is a member of the International Association of Classification Societies

Case history

Period	Instance	Result
March 2016	Court of First Instance	The Company's petition was rejected
May 2016	Court of Appeal	Court of First Instance ruling left unchanged

Position of the Atyrau Oblast Court Judicial Board for Civil Cases

The Atyrau Oblast Court ruled to leave the ruling of the Atyrau Oblast Specialised Inter-Regional Economic Court (Court of First Instance) from 3 March 2016 unchanged, and not uphold the Consolidated Supply and Services International LLP appeal. After studying case materials, the court concluded that the characteristics of the vessels imported by the Company did not meet the requirements of EEU FEA CN position 8901 90 900 0.

Deloitte recommendation
To avoid classification disputes or difficulties when declaring goods, we recommend receiving a preliminary classification from the customs authorities.

Source: *Court case reference guide of the integrated information and analytical system of judicial authorities of the Republic of Kazakhstan.*

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Recovery of payments for the use of railway wagons in the absence of an agreement between parties

Resolution of the Supreme Court Judicial Board for Civil Cases dated 13 July 2016 on case 3гп-529-16

National Company Kazakhstan Temir Zholy

Decision upholding the petition

"National Company Kazakhstan Temir Zholy" JSC (hereinafter – "the JSC") took legal action against "Bogatyr Komir" LLP (hereinafter – "the LLP") to recover payment for the use of wagons and a charge for wagon idle time.

The hearing established that:

- in March and August 2012 and between February and May 2013, the LLP was charged for the use of wagons and their downtime according to wagon supply and cleaning lists and general acts;
- the LLP receives wagons on the Promservice-Otan spur track according to Agreement № 4/41/59-AO dated 1 March 2011 to supply and clean wagons on the Promservice-Otan spur track at Ekibastuz-2 station belonging to the JSC's branch Pavlodar Technical Centre for the Processing of Transport Documents ("PTC");
- for this reason, the JSC is asking to recover the charge to the LLP for wagon use of KZT 208,663,155, KZT 4,075 for wagon downtime, and state duties of KZT 6,260,017.

After studying the case materials, the court of first instance and appeal court upheld the JSC's claims, but the court of cassation rejected them, explaining that the absence of an agreement between the parties removes any obligation the defendant may have to pay for wagon use.

Case history

Period	Level	Outcome
October 2014	Court of First Instance	JSC claims upheld
April 2015	Court of Appeal	Court of first instance ruling left unchanged
October 2015	Court of Cassation	Court of first instance and court of appeal rulings annulled and a new ruling rejecting JSC claims issued
July 2016	Supreme Court of RK	JSC claims upheld

Supreme Court of RK position

The Supreme Court of RK did not agree with the court of cassation ruling, as the parties did not dispute that railway wagons had been sent for the LLP to the Promservice-Otan spur track at Ekibastuz-2 station. It was also proved that the LLP provided duly signed applications highlighting freight transportation plans and indicating the number of wagons required, planned freight volume, freight types and the time spent by the wagons loaded.

In this context, the Supreme Court of RK upheld the court of first instance and appeal court's position as they had interpreted the term "use of wagons" to take into account subpoint 1) of point 1 of article 49 of Law *On Railway Transportation* №266 dated 8 December 2001, and a charge for the same in accordance with tariff regulations (pricing), approved by the JSC Order № 440-Ц dated 31 August 2004. The charge was based on the provision of wagons for loading and unloading in connection with written applications from the LLP, i.e. the applications assume the LLP's agreement to receive the services and do not require a specific agreement. The commitment to pay for the services arises after they have been provided, taking into consideration time, quantitative and technical parameters.

Thus, the Supreme Court of RK agreed that the essence of the dispute was justification for charging for wagon use with no agreement between the parties, while KZT 208,663,155 for the period the wagons were leased by

the LLP and the charge of KZT 4,075 for idle time was charged correctly, based on general acts, which the LLP is not disputing.

Therefore, the Supreme Court of RK established that the court of cassation ruling be annulled, that of the court of appeal should remain in force, and that the LLP should pay state duties.

Source: *Court case reference guide of the integrated information and analytical system of judicial authorities of the Republic of Kazakhstan*

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