

## LT in Focus

# The Russian Investigation Committee and the Russian Federal Tax Service developed guidelines for establishing tax evasion

In its Letter No. [ED-4-2/13650@](#) of 13 July 2017, the Russian Federal Tax Service (the FTS) released the Guidelines for establishing the taxpayers' officers' tax evasion intent (the Guidelines). The document was prepared jointly with the Russian Investigation Committee and is meant to be used by the lower tax authorities.

The document outlines the most common and aggressive tax evasion schemes that are indicative of tax offence premeditated by taxpayer's officers and contains the guidelines for (1) identifying the intent to commit a tax offence and (2) recording the tax audit findings. Attached to the Guidelines is a list of questions that the local tax authorities must ask the taxpayer's employees that are liable to criminal prosecution for tax offences (Articles 199, 191.1, and 199.2 of the Russian Tax Code).

Read on for an overview of the key recommendations and comments from our subject-matter experts.

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### Concept and consequences of intent in tax offences

The Guidelines establish the relation between an unjustified tax benefit and the intent to receive it. According to the document, the non-payment or partial non-payment of tax, entailing the receipt of an unjustified tax benefit from an imitation of genuine business operations or contractual relations, use of shell companies, sham asset spin-off or unjustified use of tax benefits most likely attest to the taxpayer's intent, which, therefore, entails the application of Item 3, Article 122 of the Russian Tax Code.

Unlike Item 1, Article 122 of the Russian Tax Code that envisages penalties of 20 percent of the outstanding tax amount, intentional tax offence is subject to a 40-percent penalty. The document serves as a guidance for the local tax authorities that need to investigate the taxpayer's intent even if there are no grounds to initiate criminal prosecution and a shift towards qualifying the taxpayer's actions under Item 3, rather than Item 1, Article 122 of the Russian Tax Code may well be expected, especially in disputes over mala fide vendors.

Furthermore, the tax authorities are advised against citing the extenuating circumstances when considering intentional tax offences – which looks somewhat controversial. Article 112 of the Russian Tax Code does not name the lack of intent as a prerequisite for citing the extenuating circumstances. Furthermore, there is no consistency on this issue in the court practice. We expect the courts to be reversing the tax authorities' opinions, disallowing the mitigating circumstances.

### Proof of intent

The FTS and the Investigation Committee suggest proving lack of randomness in the (chain) of events and actions attributable to an offence as a standard of proof of intent.

The Investigation Committee and the FTS also underline that the evidence set forth in a tax audit report shall unequivocally indicate that a taxpayer's wrongdoing is not a result of financial or tax accounting errors, but a premeditated conscious action of a taxpayer or third parties acting on its behalf. The tax authorities are also recommended to be guided by the style used for indictments in criminal proceedings. According to the Investigation Committee and the FTS, such wording as "aggressive tax planning", "mala fide taxpayer", "failure to exercise due diligence" do not correlate with the task of proving the intent.

The Guidelines are aimed at facilitating the investigation authorities' efforts to identify the intent in non-corporate tax offences.

## Intent to evade tax: examples

The Guidance gives examples of the circumstances that would be indicative of intentional tax offences, namely:

- 1) Concerted actions by related parties
- 2) Taxpayer's involvement in a tax evasion scheme
- 3) Taxpayer's controlling interest in a shell company
- 4) Imitation of business relations
- 5) Complex and non-transparent actions that would not have been performed as part of ordinary activities
- 6) Direct evidence of a tax evasion scheme
- 7) Taxpayer's further wrongful conduct.

The Guidelines emphasise that if a taxpayer is found to

enter into arrangements with a shell company, the fact of control over such shell company by a taxpayer accused of an offence as per Item 3, Article 122 of the Russian Tax Code must be proven. The recommendation is consistent with the new provisions of Item 3, Article 54.1 of the Russian Tax Code, setting forth that a tax offence committed by a taxpayer's counterparty will only be considered proving the wrongfulness of the reduction of its taxable income and/or tax payable if the fact of control over the shell company or the pre-agreement between them is established.

Nevertheless, the FTS recommends paying attention to the taxpayer's possible imitation of performing the appropriate counterparty integrity check and analysing both the circumstances evidencing the pre-agreement with such counterparty and the due care exercised by the taxpayer in selecting the counterparty.



**Alexei Sergeev**  
Senior Manager  
Tax Dispute Resolution

***"The Guidelines recommend collecting and storing the potential evidence of a taxpayer's intent to commit a tax offence as early as at the tax audit stage. As evidenced by the existing practice, the tax authorities seldom identify taxpayers' wrongful intent during the tax audits, therefore, the most common sanctions are penalties of 20 percent of outstanding tax (Item 1, Article 122 of the Russian Tax Code). The intent, if proven, raises the penalty to 40 percent (Item 3, Article 122 of the Russian Tax Code)."***

***If intent is discovered in a corporate taxpayer's actions, it can likely entail criminal prosecution of the taxpayer's officers as pursuant to Item 4, Article 110 of the Russian Tax Code, the fault of a company depends on the fault of its officers. Conversely, the taxpayer's fault proven by a tax audit implies that its officers are guilty of committing a tax offence. Criminal prosecution is initiated only if the wrongful intent of a particular individual is proven. Proving an intent in a tax offence used to be quite challenging for the investigation authorities and often resulted in a termination of criminal proceedings due to their failure to prove such intent. The Guidelines are now expected to facilitate the process".***

## Verifying and documenting the intent

To enable application of Item 3, Article 122 of the Russian Tax Code and further criminal prosecution, a tax audit report must set forth the taxpayer's officers' tax evasion intent. Therefore, the tax authorities shall put together a list of officers whose actions have led to a tax offence, analyse their roles and responsibilities and the availability of "external" sources attesting to the intent.

According to the Guidelines, the re-questioning and interrogation of officers aimed at identifying the contradicting testimonies would be an effective tool to discover the at-fault party. The tax authorities are recommended to use the interrogation methods applied by the investigation authorities, which actually means carrying out cross-examination during tax audits. In view of the above, the taxpayers must prepare to field audits in terms of aligning the conduct of their officers and employees during interrogations.

The Guidelines set forth a list of priority tax control activities that must be carried out by the tax authorities to prove the most common tax evasion schemes. The tax authorities are also recommended to engage the investigation authorities in the examination of offices and territories which is yet another way to put pressure on a taxpayer.

If premeditated arrangements involving sham transactions with shell companies or affiliates are discovered, the tax authorities may, on top of the mandatory accounting documents, demand any other documents that may prove a relationship between the taxpayer and such shell companies and the taxpayer's awareness of selecting a mala fide counterparty. It primarily concerns internal correspondence between the employees, the incoming correspondence, the results of advisory services, including audit and legal services outsourced by the taxpayer.

Given that the draft law entitling the tax authorities to request the documents received by audit firms during their engagements passed first reading on 23 June 2017 (Draft Law No. 96436-7), the taxpayers should pay special attention to the appropriate internal controls over the document management both in the head office and the branches.

The Guidelines recommend that interrogations cover the widest possible scope of people (employees of the taxpayer and its affiliates, accountable officers, employees that received large cash advances in a tax period, the taxpayer's outsourcers). The document underlines the importance of interrogating the former employees, therefore, the HR policies should also be of a matter of special attention for the companies.

The Guidelines recommend engaging the investigation authorities to establish the relation between the parties. The data on shared preparation and filing of tax returns obtained during the investigation (through checking IP addresses used to file the returns or make settlements in accounting systems) will have special weight in proving such relation.

The investigation authorities shall also be involved in examining offices and sites, retrieving documents and

other evidence, such as stamps, letterheads, flash memory devices, servers, tokens, rutokens.

The Guidelines also underline the importance of cooperation between the tax authorities and other government bodies, such as the Central Bank of Russia, Rosfinmonitoring, Gostekhnadzor, Road Traffic Police, Rospatent and other registration authorities that may have information relevant for proving the intent, e.g., cash flow statements.

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## Deloitte's comments

The release of the Guidelines expectedly continues the implementation of the government's fiscal policy, aimed at securing the fiscal interests of the state.

According to the experts, the Guidelines signify an increasing pressure the controlling authorities exert on the business. Thus, according to the IPT Group, nearly 78 percent of the Russian taxpayers have felt stronger tax administration pressure from the state in 2016-2017<sup>1</sup>.

The situation becomes even more challenging with the adoption of Federal Law No. 163-FZ "On amendments to Part I of the Russian Tax Code" which, compared to Russian Supreme Court Plenum Ruling No. 53, pursues a tougher approach to unjustified tax benefits.

New Article 54.1 of the Russian Tax Code will apply to desk audits of tax returns filed after 19 August and field audits scheduled after this date. Given that the FTS and the Russian Investigation Committee have officially announced the intention to cooperate in unjustified tax benefit cases,

the tax audits governed by the amended provisions of the Russian Tax Code will inevitably entail an increase in criminal prosecution of tax offences and investigation activities on the taxpayers' sites.

Furthermore, the tax authorities may well shift towards universally applying Item 3, Article 122 of the Russian Tax Code, envisaging a 40-percent penalty, which may be a negative development for the taxpayers that do not carry out aggressive tax planning through arrangements with shell companies and other wrongful schemes.

The tax evasion schemes set out in the Guidelines and posted on the FTS website<sup>2</sup> are textbook examples rather than real-life case studies. Therefore, the courts are expected to develop more complex approaches to proving the intent of obtaining unjustified tax benefit in less straightforward situations than those described in the Guidelines, which also may entail broader application of Item 3, Article 122 of the Russian Tax Code.

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We hope that you will find this newsletter interesting and informative. Should you have any questions, please refer to your regular Deloitte contacts or Alexei Sergeev.

Kind regards,

**Deloitte CIS Partners**

<sup>1</sup> <http://www.forbes.ru/biznes/348367-riski-dlya-biznesa-78-rossiyskih-kompaniy-zayavlyayut-o-roste-davleniya-so-storony>

<sup>2</sup> [https://www.nalog.ru/rn77/taxation/reference\\_work/conception\\_vnp/](https://www.nalog.ru/rn77/taxation/reference_work/conception_vnp/)

# Contacts

## Tax & Legal



**Alexei Sergeev**  
**Senior Manager**  
Tax Dispute Resolution  
[alsergeev@deloitte.ru](mailto:alsergeev@deloitte.ru)

## TaxSmart app



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