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LT in Focus

Tax Disputes and Litigation Review: Issue №7

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Introduction

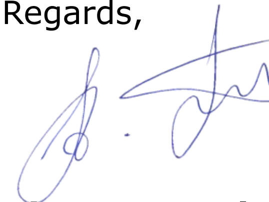
We keep our finger on the pulse of your business

Dear friends

We are happy to offer this latest overview of court practices around Kazakhstan court tax disputes. In it we have considered the most interesting and significant cases that may have the potential to impact any aspect of your business.

Should you be interested, we would be happy to have a more detailed discussion on any of the cases considered in this **LT in Focus**, or any question you may have on the latest tax court practices, including investment disputes.

Regards,



Dispute Resolution Group

Tax disputes

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Tax audit appeals

Astana Court Decision dated 7 March 2018 on a claim from X LLP

Recognition of the notification of tax audit results as illegal and its cancellation

X LLP (the "**Taxpayer**") took the West-Kazakhstan Oblast State Revenue Department (the **"Department"**) to court to have Notification #124/1 dated 13 November 2017 recognised as illegal and cancelled. The Department had accrued value added tax ("**VAT**") of KZT 3,195,955, identified a VAT overrun that had been returned from the budget, but not confirmed as such, of KZT 933,263 and charged interest of KZT 829,326.

The Taxpayer believes that the Department incorrectly disallowed VAT offset on contractor invoices for compensation for equipment lost while drilling a well and for a paid contractual bonus, because it did not take into account that an agreement between the Taxpayer and contractor contains a provision whereby lost equipment is compensated by the Taxpayer, which means the compensation should be included in the agreement value and treated as subsoil costs.

The equipment was lost while drilling the well, and for that reason became a component of the well, and as such, became the Taxpayer's property.

The bonus paid to the contractor is also part of the agreement value and paid monthly as contractor motivation.

For this reason the agreement parties charged VAT on the compensation and bonus payments, and as they were (and are) parts of the agreement value, the Taxpayer legally offset the VAT paid on them.

However, the Department believes the notification is legal and that the Taxpayer's arguments should be disregarded because the lost equipment belongs to the contractors, is used in its operations and as such is used to generate its taxable turnover.

In addition, according to tax law in effect when the Department disallowed the VAT, any VAT offset should be disallowed if goods are damaged or lost.

Therefore, after losing the equipment, the contractor should have corrected the offset VAT. The contractor did not sell the equipment and for that reason was not entitled to charge VAT on it. The bonus cannot be considered a service and for that reason cannot be used as taxable turnover, as it is not a part of the agreement value, rather a motivational measure.

As a result of the above, the Department believes the notification is lawful and should be cancelled in court.

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Tax audit appeals

Period	Instance	Ruling
March 2018	Court of first instance	In favour of the Department
May 2018	Court of appeal	Court of first instance decision upheld

Position of the court of first instance

The court decided that the notification was lawful because:

- VAT can be offset only when goods, work or services are actually received, used or are to be used for taxable turnover purposes.
- In this case payments for lost equipment do not qualify as goods, work or services received. Furthermore, the purpose of the equipment was not to increase the well value.
- The bonus is only a motivational measure, and it cannot be considered as a payment for executed work, or as received goods, executed works, services.

Position of the court of appeal

The court of first instance decision was recognised as legal and was upheld. The Taxpayer's appeal was rejected.

More details

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Tax audit appeals

Astana Court Decision dated 3 September 2018 on a claim from X LLP

Recognition of the notification of tax audit results as illegal and its cancellation

X LLP (the "**Taxpayer**") took the West-Kazakhstan Oblast State Revenue Department (the **"Department"**) to court to have Notification #188/1 dated 18 May 2018 recognized as illegal and cancelled. The Department had accrued value added tax (**"VAT"**) of KZT 20,720,963, identified a VAT overrun that had been returned from the budget, but not confirmed as such, of KZT 15,077,554, and charged interest of KZT 2,719,707.

The Taxpayer believes that the notification is unlawful because the Department came to the wrong conclusion regarding the eligibility of VAT under invoices for reimbursable expenses (transportation, accommodation and others) for offset, since they had been included in the agreement value and as such as subject to VAT. The Taxpayer is entitled to further offset VAT paid under the given invoices. Moreover, transporting staff to their place of work and providing them with accommodation was a necessity, because otherwise the contractor would not have been able to perform its contractual obligations.

The justification for including the given expenses in a taxable turnover, and offsetting VAT paid on them, was confirmed by the tax authorities in written clarifications and also by juridical practice.

The Department, however, insists that the notification is legal because reimbursable expenses cannot be considered as services received for taxable turnover purposes as contractually they are not included in the cost of services and subsequently VAT of KZT 20,721,000 could not be offset by law.

For this reason, the VAT returned from the budget and not confirmed as such should be repaid.

Period	Instance	Ruling
September 2018	Court of first instance	In favour of the Department

Position of the court of first instance

The court decided that the notification was lawful because:

- Interpreting the agreement literally, the agreement value consists of the number of hours worked multiplied by appropriate rates, which means that the reimbursable expenses cannot be considered a part of the agreement value.

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- Point 6.12 of the agreement prescribes the contractor's right to demand compensation for contractor staff transportation and accommodation expenses, which arose during the execution of the agreement. The Taxpayer agreed with this provision, and, at its own risk and discretion, accepted the obligation to reimburse the contractual expenses that were not part of the agreement value.
- Moreover, the expenses to provide staff with transportation, travel tickets, accommodation, catering and communication service are not recognised as the Taxpayer's taxable turnover.

The court of first instance upheld the Department's position and rejected the Taxpayer's claim.

More details

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Desktop audit appeals

Specialised Interdistrict Economic Court Ruling dated 23 August 2018 on a claim from X LLP

Recognition of notifications issued after a desktop review (cameral control) as illegal and their cancellation

X LLP (the "**Taxpayer**") took the Atyrau State Revenue Office (the **"Tax Office"**) to court have Notifications #151080800080 and #151080800081 dated 27 April 2018 from a desktop review (cameral control) recognised as illegal and cancelled.

The Taxpayer believes that the Tax Office was not authorised to issue the notifications as it had already issued notifications with respect to the same violations, which the Taxpayer had settled.

Furthermore, the Tax Office failed to observe the statutory period for issuing notifications.

Position of the court of first instance

The court did not consider the case on its merits and terminated proceedings because:

- The Taxpayer had disputed the notifications with a higher tax authority

The Taxpayer disagreed with the court ruling and appealed it in the court of appeal.

The Taxpayer pointed out the following in its appeal:

- The court of first instance, in terminating case proceedings, followed provisions in the version of the Tax Code from 10 December 2008, when the notifications were issued in 2018 according to a newer code – the Tax Code dated 25 December 2017.
- The sections of the new code governing the process for executing notifications from a desktop review (cameral control) differ significantly from those in the Tax Code dated 10 December 2008.
- Unlike the Tax Code dated 10 December 2008, the new Tax Code does not consider appealing notifications with a higher tax authority as one of the ways to execute them.
- Based on the above, the notifications have still not been executed, which means the court ruling is unlawful and should be cancelled.

Period	Instance	Decision
August 2018	Court of first instance	Case proceedings were terminated
October 2018	Court of appeal	Ruling upheld

Position of the court of appeal

- The court of appeal considered the court of first instance ruling as lawful and rejected the Taxpayer's appeal.

More details

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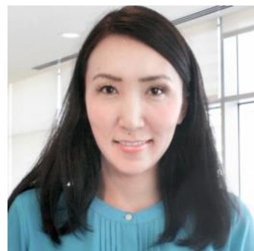

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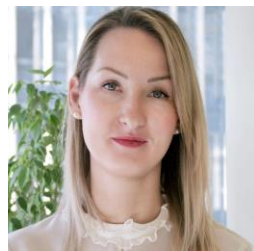

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