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On legal regulation of tax optimization and tax evasion in Ukraine

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Problem statement. Nowadays in Ukraine, there are more and more situations where individuals engaged in entrepreneurial activity, try to use any legal options to reduce their tax liability. The right of a taxpayer to carry out such actions is beyond doubt and is based on the constitutional principle of equality of all forms of ownership. But such actions frequently cause negative reaction from the government through its fiscal authorities, since tax optimization model is often developed on the edge of legality. On the one hand, the state tolerates legal reduction of tax liability by providing various tax concessions and establishing different tax regimes, on the other hand, law enforcement, including judicial, practice restricts such actions by introducing the concept of “abuse of rights” and “unfair practices” within tax relations. In this regard, the definition of tax optimization, its support in tax legislation of Ukraine, and clear differentiation between tax optimization and other forms of the reduction of tax liability, including tax evasion, are becoming more important.

Overview of relevant research. The topicality of the research is evident due to the close interest in the problem by academia. Despite the importance of the problem, there are few fundamental works on the principles of legal grounds of tax optimization, whereas most research is fragmented and concerns certain aspects of the phenomenon. The science of tax law has not yet formed a unified approach to understanding tax optimization. This phenomenon is often equated with other categories of tax law, such as tax planning, tax minimization, etc. There is no clear distinction between these phenomena, including the differentiation between tax optimization and tax evasion. Our research lies within the context of theoretical works by Arkadiy Bryzgalin, Borys Myshkin, Learned Hand, Denys Shchokin, and others.

The aim of the research is to show the importance of legislative regulation of the problem and to develop clear criteria for differentiating between tax optimization and related categories of tax law in order to restrain discretion in this matter exercised by law enforcement, fiscal authorities and courts in particular, as well as reveal the main approaches to the definition of the concept within the science of tax law.

Discussion. Tax optimization is a relatively recent phenomenon. It became wide-spread in 1920s, when WWI and the need to eliminate the consequences it caused led to a significant increase in the tax burden on taxpayers, who, in their turn, began searching actively for the ways to minimize it¹. Today the right to tax optimization is seen as an inalienable right of a taxpayer, and the words of a United States judge Learned Hand has become popular with both taxpayers and scholars: “there is nothing sinister in so arranging one’s affairs as to keep taxes as low as possible. Everybody does so, rich or poor; and all do right, for nobody owes any public duty to pay more than the law demands [...]”². Nevertheless, it is very

¹ І.І. Бабін, *Податкова оптимізація як категорія податкового права*, “Науковий вісник Чернівецького університету” 2015, Випуск 765 Правознавство, р. 103.

² *Gregory v. Helvering*, 293 U.S. 465 (1935).: <https://supreme.justia.com/cases/federal/us/293/465> (access 1.02.2017)

difficult to demarcate tax optimization, to distinguish it from other ways to minimize taxes (e.g., tax evasion, circumvention of tax laws).

In the science of tax law there are radically different views on the notion of tax optimization. According to Borys Myshkin, tax optimization is a reduction of the tax liability by means of well-directed lawful efforts of taxpayers, including their full use of all the tax concessions provided by law, other legal ways and means, taking into account the interests of the state³. However, taking into account the interests of the state in tax optimization makes no sense at all, since the interests of the state in tax relations is quite obvious – to get the maximum possible amount of taxes. If taxpayers plan their activities so as to pay the maximum amount of taxes in the end, what kind of tax optimization is it? Therefore, the abovementioned understanding of tax optimization within the science of tax law is rather the exception than the general rule. A more common definition of tax optimization is as follows: a reduction of the tax liability by means of well-directed lawful efforts of taxpayers, including their full use of all the tax concessions provided by law, immunity from taxes, and other legal ways and means⁴. But this definition of tax optimization cannot fully reflect the essence of the phenomenon. Since tax optimization is all about taxpayers doing what is legal only. At the same time Article 19 of the Constitution of Ukraine provides that “The legal order in Ukraine shall be based on the principles according to which no one shall be forced to do what is not stipulated by law”, establishing the principle that “everything that is not prohibited by law is allowed.” Thus, the main difference between tax optimization and tax evasion is taxpayers using permitted, or not prohibited, by the legislation ways to reduce the amount of tax payments without violating the law. In this respect, such actions on the part of taxpayers are not a tax offense or crime, and therefore does not entail adverse con-

³ Б.В. Мышкин, *Налоговая оптимизация как проявление налоговой правосубъектности*. – Дис. канд. юрид. наук, Москва 2004, р. 68.

⁴ А.В. Брызгалин, В.Р. Берник, А.Н. Головкин, *Налоговая оптимизация: принципы, методы, рекомендации, арбитражная практика*, Екатеринбург 2002, р. 23.

sequences for the taxpayers, such as additional tax payments, and the imposition of fines and penalties on arrears.

Tax evasion is a criminal offense, whose *corpus delicti* is defined by Article 212 of the Criminal Code of Ukraine (hereinafter – the CCU) as willful evasion of taxes, fees or other compulsory payments which are part of the taxation system established by law, by an official of an enterprise, institution or organization of any ownership status, or by any unincorporated entrepreneur, or by any other person liable to pay such taxes, fees or other compulsory payments.

That article provides for criminal liability not for the fact of non-payment of taxes in due time, but for willful evasion of their payment. In this regard, the Court must determine that the person intended to not pay taxes, fees or other compulsory payments in full or a part of them⁵.

The intent to evade taxes may be evidenced by, for example: the absence of tax accounting records or keeping them in violation of the established order; distortions in accounting or reporting documents; not posting the cash received for work carried out or services provided; having double-entry book-keeping (official and unofficial); use of bank accounts, which have not been reported to the Tax Authorities; overstating actual expenses included in cost of sales, etc.

The objective side of the offense is the taxpayer's failure to comply with the obligations imposed by the Tax Code of Ukraine, if such actions resulted in actual non-receipt of significant, large or particularly large amounts of funds by budgets or special state funds (which respectively exceed 1000, 3000, 5000 tax-free minimum incomes established by law). However, the methods of avoiding or neglecting of these obligations are not listed in the disposition of Article 212 of the CCU, therefore there are no guarantees that the actions of the taxpayer aimed at optimizing tax liability using means not prohibited by law shall not be qualified as tax evasion. In practice, the actions of the kind, among other things, include: failure to submit documents related to the calculation and pay-

⁵ А.В. Шевчук, М.Д. Дякур, *Кримінальне право України (Особлива частина)*. Навчальний посібник, Чернівці 2013, pp. 136–137.

ment of taxes, fees and other compulsory payments; concealment of taxable items; understatement of taxable items; understatement of taxes and other compulsory payments⁶. Thus, the classification of a taxpayer's action to reduce the tax liability as tax optimization or evasion of taxes largely depends on the discretion of fiscal authorities and courts. In the Unified Register of pre-trial investigations in an average month there are nearly 277 criminal proceedings under Article 212 of the CCU. At the same time, on average 18 indictments are issued per month, which is only 6.5% of the total number of proceedings recorded monthly. And 26 proceedings, on average, are submitted to court with the request for exemption from criminal liability per month, accounting for 9.4% of the total number of proceedings recorded monthly. From the abovementioned we can conclude that:

- either the officials of the Ministry of the Interior and/or the prosecutor's office cannot conduct the investigation and comply with statutory deadlines;
- or the official note of the tax inspector to the investigation department of the tax authority reporting the offense is knowingly false, i.e. defamatory, and is used to exert pressure on taxpayers and their officials⁷.

It should be noted that in the letter dated December 11, 2013 number 1713/12/1313 the High Administrative Court of Ukraine drew attention to the legal stance of the appellate court in the respective category of disputes, which was expressed in the resolution of the Supreme Administrative Court of Ukraine of November 19, 2013, passed in the hearing of the case number 2a-7912/12/1370. This stance is that regulatory authorities can find the transaction knowingly adverse to the interests of the state and society by regulatory authorities only in terms of whether the transaction is contrary to the relevant fiscal interests of the state, which the

⁶ Постанова пленуму Верховного Суду України “Про деякі питання застосування законодавства про відповідальність за ухилення від сплати податків, зборів, інших обов’язкових платежів” від 08.10.2004р. №15.: <http://zakon5.rada.gov.ua/laws/show/v0015700-04> (access: 1.02.2017)

⁷ *Податковий спір чи злочин?*, Київ 2013, pp. 44–45.

regulatory authorities protect. In any other case the analysis of whether the transaction complies with current legislation, including whether it contradicts the interests of the state, is outside the competence of regulatory authorities. The above applies to the respondent's assessment of whether the parties to controversial business transactions complied with the legislation on the regulation of the financial services market. The possible failure to comply with other branches of law when making transactions, which mediated the controversial business transactions, does not evidence of the tax-evasive nature of the transactions⁸.

Analyzing this approach, we should address the position of the Supreme Administrative Court of Ukraine of November 14, 2012, which greatly enhances the protection of taxpayers from unwarranted accusations from tax authorities. The resolution of the case number K/9991/50772/12 concerns the recognition of transactions void⁹. The position of the Court is that even when the transaction appears to have the signs of worthlessness, tax authorities can only file a recovery lawsuit stating the worthlessness of the transactions to collect the funds received from these transactions, deliberately conducted contrary to the interests of the state and society, as revenue.

The legal definition of tax optimization and the legal provision of the criteria for differentiating between tax optimization and tax evasion will essentially enable the taxpayers to plan their activities and the fiscal authorities and courts to classify these activities¹⁰. The first attempts at such a differentiation can be seen in paragraph 5 of the German imperial decree "On Taxes and Fees" of

⁸ Інформаційний лист Вищого адміністративного суду України від 11.12.2013 р. № 1713/12/13–13: <http://zakon4.rada.gov.ua/laws/show/v1713760-13> (access: 1.02.2017)

⁹ Постанова Вищого адміністративного суду України по справі № К/9991/50772/12 стосовно визнання угод недійсними від 14.11.2012р.: <http://document.ua/pro-viznannja-nechinnim-ta-skasuvannja-podatkovogo-povidomle-doc122304.html> (access: 1.02.2017)

¹⁰ І.І. Бабін, *Презумпції та фікції в податковому праві: Навчальний посібник*, Чернівці Рута, 2009, р. 210–212.

1919 (Reichsabgabenordnung): “The obligation to pay taxes cannot be bypassed or reduced because of the abuse of civil structures and legal means”¹¹. But this provision was subjected to harsh criticism. Some even doubted its appropriateness, as it was applied infrequently. Discussions boiled down to the question of whether the existence of rules that provide too much discretion, and the application of which depends entirely on the subjective appreciation, as well as of the impossibility of a clear distinction between the right to tax savings and illegal ways to avoid paying taxes. As amended, the rule qualifies as abuse when the taxpayer opts to execute the transaction in such a way that enables the taxpayer or a third party to receive non-statutory tax benefits that would not have occurred if the taxpayer had executed the transaction in correspondence to its economic results¹².

According to Gerd Leng, today in the world practice there are two basic approaches to differentiation between lawful and unlawful reduction of the tax burden. The first approach is the introduction into tax legislation of the general principles for demarcating lawful and unlawful reduction of tax burden, such as the business goal, compliance with the spirit and letter of the law, and others. Effective application of these principles in practice require a high level of training among tax officials and judges. The second approach is the introduction into tax legislation of special rules to counter a specific tax scheme¹³.

Most continental European countries favor the first approach, having included the rules (principles) for legitimate tax planning into their national tax codes. The respective provisions have also been enacted in Canada, Australia, New Zealand and South Africa, while in other countries with similar legal tradition (especially the

¹¹ Reichsabgabenordnung vom 13. Dezember 1919, Reichsgesetzblatt 1919, Nr. 242, p. 1993.

¹² Abgabenordnung in der Fassung der Bekanntmachung, Bundesgesetzblatt 18 Dezember 2013, p. 4318.

¹³ Г. Ленг, *Законное и незаконное снижение налоговых платежей: постановка проблемы и подходы к ее решению*, “Налоговая политика и практика” 2005, №2, p. 7.

UK and the US) the doctrinal sources are deemed adequate (“the judges shall decide” approach)¹⁴.

In Ukraine, the foundation has been laid for the second approach differentiation between lawful and unlawful reduction of the tax burden. The Tax Code of Ukraine contains special rules to counter specific tax schemes of tax evasion¹⁵. But the legal relations that form the basis for tax administration, are extremely dynamic, and they often outrun the changes to tax legislation aimed at countering tax evasion. Hence including into the Tax Code of Ukraine the general principles of differentiation between tax optimization and tax evasion would guide fiscal authorities and courts in the right direction. In the science of tax law there is also an approach according to which tax optimization is a manifestation of the legal rule on conflict of interests which states that all the contradictions of legislation on taxes must be interpreted in favor of the taxpayer¹⁶. The provisions of paragraph 4.1.4 of Article 4 of the Tax Code of Ukraine lay the basis for this stance providing for the presumption of lawfulness of taxpayer’s decisions if the law or other normative act issued pursuant to a law, or if the rules of different laws or different normative acts allow for ambiguous (multiple) interpretation of the rights and obligations of taxpayers or regulatory authorities, thus providing the means to decide in favor of the taxpayer as well as the regulatory authority.

Moreover, we should note the fact that tax optimization is seen solely as a set of well-directed actions of the taxpayer. Naturally, the taxpayer is the party whose interest in reducing tax liability is the greatest. But the state establishing tax concessions or other legal ways to reduce the tax burden expects them to be used. Otherwise what is the point in creating a tax concession if it no one will use?

¹⁴ Т.А. Гусева, *Налоговое планирование в предпринимательской деятельности: правовое регулирование*: Монография, 2-е изд., перераб. и доп., Москва 2007, pp. 84–100.

¹⁵ І.І. Бабін, *Податкове право України*: Навчальний посібник, вид. 2-ге, виправл. та доповн., Чернівці 2013, pp. 204–207.

¹⁶ И.Н. Соловьев, *Уклонение от уплаты налогов и оптимизация налогообложения*, “Налоговый вестник” 2001, №9.: <http://www.nalvest.com/nv-articles/detail.php?ID=25343> (access: 1.02.2017)

However, many taxpayers who are eligible for tax concessions, do not use them. The reason is not their unwillingness to use the tax concession, but ignorance of the existence of such a concession. If the tax concession has not been declared in the tax return, it does not mean that the taxpayer does not agree to its use. The assumption that the taxpayers always agree to the maximum possible use of tax concessions, as this reduces the seizure of their property. In this regard, if the taxpayer did not claim a tax benefit in the tax return, it does not necessarily mean that the taxpayer waived it, until the direct will of the taxpayer proves otherwise. The purpose of the fiscal authorities is not maximizing tax revenue, but monitoring the compliance with the tax laws, the accuracy of calculation, completeness and timeliness of revenue received by the budget. The accuracy of tax calculation involves not only accounting the responsibilities of taxpayers, but to no lesser degree informing them of tax concessions, rebates and other lawful ways to reduce tax liability. Tax legislation of some countries directly provides the responsibility of the tax authority to take into account the taxpayer's concessions during the inspection. For instance, in accordance with paragraph 5 of Article 149 of the Tax Code of the Russian Federation the taxpayer is can waive a number of exemptions from VAT, only by submitting a waiver of privileges to the tax authority. Denis Shchokin states that this legal mechanism of waiving is an expression of the presumption of consent of the taxpayer to the tax concession, which can only be overturned by the taxpayer's direct will¹⁷.

Conclusions. Summing up the above, it should be noted that tax optimization is a complex and ambiguous phenomenon. Neither tax legislation, nor its practical application, nor the science of tax law outline its clear boundaries and criteria for the demarcation of lawful and unlawful reductions of tax liability. The tax system of Ukraine is only beginning to receive proper legal and institutional framework, thus the analysis of the experience of foreign countries, development our own approaches to understanding of tax optimi-

¹⁷ Д.М. ЩЕКИН, *Юридические презумпции в налоговом праве: Учебное пособие*, Москва 2002, р. 235.

zation and differentiation between lawful and unlawful reductions of tax liability remain burning issues.

STRESZCZENIE

Problemy prawnej regulacji optymalizacji podatkowej i unikania opodatkowania na Ukrainie

W artykule analizie poddana została regulacja prawna optymalizacji podatkowej i unikania opodatkowania na Ukrainie. Prawo podatnika do korzystania z wszelkich możliwości prawnych, aby zmniejszyć swoje zobowiązanie podatkowe, opiera się na konstytucyjnej zasadzie równości wszystkich form własności. Takie działania mogą jednak często spowodować negatywną reakcję ze strony rządu za pośrednictwem organów podatkowych, ponieważ modele optymalizacyjne są często opracowane na granicy legalności. Z jednej strony państwo toleruje obniżenie prawnego zobowiązania podatkowego poprzez różnego rodzaju ulgi podatkowe i tworzenie różnych systemów podatkowych, z drugiej strony organy ścigania, w tym sądowne, ograniczają takie działania poprzez wprowadzenie pojęcia „nadużycia prawa” oraz „nieuczciwych praktyk” w stosunkach podatkowych. Dziś każdy kraj opracowuje własne podejście do różnicowania między legalnymi a nielegalnymi metodami zmniejszenia obciążeń podatkowych.

Definicja optymalizacji podatkowej, jego konsolidacji w przepisach podatkowych Ukrainy oraz ustanowienie jasnych granic pomiędzy optymalizacją podatkową i innymi formami zmniejszenia zobowiązań podatkowych staje się coraz ważniejsze. W artykule autorzy pokazują wady braku prawnego uregulowania problemu na Ukrainie i prezentują główne podejścia do definicji tego pojęcia w nauce prawa podatkowego.

Słowa kluczowe: prawo podatkowe; przepisy podatkowe; podatek; podatnik; zobowiązanie podatkowe; obciążenie podatkowe; optymalizacja podatkowa; Ukraina

SUMMARY

On legal regulation of tax optimization and tax evasion in Ukraine

The article analyzes the legal regulation of tax optimization and tax evasion in Ukraine. The right of a taxpayer to use any legal options to reduce their

tax liability is based on the constitutional principle of equality of all forms of ownership. However such actions frequently cause negative reaction from the government through its fiscal authorities, since tax optimization model is often developed on the edge of legality. On the one hand, the state tolerates legal reduction of tax liability by providing various tax concessions and establishing different tax regimes, on the other hand, law enforcement, including judicial, practice restricts such actions by introducing the concept of “abuse of rights” and “unfair practices” within tax relations. Today, each state develops its own approach to differentiation between lawful and unlawful reduction of the tax burden.

The definition of tax optimization, its consolidation in the tax legislation of Ukraine and the establishment of clear boundaries between tax optimization and other forms of reduction of tax liability, including tax evasion, are becoming increasingly important. In this article, the authors show the shortcomings of absence of legislative regulation of the problem in Ukraine, and reveal the main approaches to the definition of this concept in the science of tax law.

Keywords: tax law; tax legislation; taxpayer, tax liability; tax burden; tax optimization; tax evasion; Ukraine

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