

## Trends of the Tax Control of Transactions between Related Parties in the Russian Federation

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### Abstract

The Russian economy is a part of the world economy, and many business entities carry out activities both in Russia and abroad with the use of various international structures: holdings and transnational corporations. Development of such structures within the context of competition between tax systems of different countries, can lead to significant losses for the state budget, which are caused by the withdrawal of profit centers to countries with a more favorable (preferential) tax regime. As a result, the Russian legal system inevitably develops within the mainstream of world trends and adapts to more and more complicated ways and methods of conducting economic activity. One of the characteristic trends in the development of Russian legislation is the development and implementation of legal institutions that, through international tax planning methods, make it possible to prevent tax evasion. Such institutions are already operating in the legal systems of developed countries. At the present stage of economic development of countries, one of the most relevant is the institution of tax control of transactions between interdependent persons. The relevance of the topic of the paper is the definition by the authors of the paper of the term "tax control of transactions between interdependent persons, as well as identification of changes reflecting the evolution of tax control of transactions between interdependent persons in the Russian Federation.

**Keywords:** Tax Control of Transactions between Interdependent Persons, Transfer Pricing, 227-FZ, Tax Legislation

### Introduction

Tax control is one of the main elements of state control of a market economy. In a broad sense, tax control means a set of measures for state regulation of the economy aimed at the effective implementation of the economic policy of the Russian Federation and ensuring fiscal interests of the state [1]. In the narrow sense, the tax control means a special type of activity of authorized state bodies aimed at obtaining information on compliance with the norms of tax legislation and checking the completeness and timeliness of tax obligations fulfillment. An integral part of the state tax control is the tax control of transactions between interdependent persons [2].

### Materials and Methods

In Russian scientific practice the term "tax control of transfer pricing" prevails, and the term "tax control of transactions between interdependent persons" is used as the title of section V.1 in the Tax Code of the Russian Federation. Despite the fact that on the whole these are similar terms, at the same time they cannot be identified with each other, since the term should reflect the legal and economic specifics of Russian realities. In connection with this logical assumption, the analysis of approaches to the definition of the term "tax control of transfer pricing" and the synthesis of the term "tax control of transactions between interdependent persons" on its basis are considered as appropriate.

L. F. Sultanova and R.I. Bagautdinova consider that the tax control of transfer pricing is the activity of state bodies, which consists in obtaining adequate amounts of taxes by the state that are associated with the use of market prices [3]. This definition, in a simplified form, characterizes the tax control of transfer pricing, but does not take it into account in terms of systemic nature.

According to N. M. Izmailov and A. V. Soldatenko, tax control of transfer pricing is one of the key areas for the tax authorities, which consists in countering the use of transfer prices for evading taxes and withdrawing profits from the Russian Federation. It can be noted that this definition of the term "tax control of transfer pricing" is significantly expanded in comparison with the first, but also does not describe the entire complexity of this term.

AsL. P. Grundel puts it, tax control of transfer pricing is one of the important directions of the state tax policy, the purpose of which is to ensure the counteraction to the use of transfer prices by interdependent organizations with a view to minimizing taxes [5]. At the same time, transfer pricing can be applied not only between interdependent organizations, but also between interdependent organizations and individuals, and between individuals. According to V.A. Shapovalov, tax control of transfer pricing is an activity that consists in ensuring fair market pricing by clarifying the list of interdependent persons, controlled transactions, and the development of mechanisms for tax control in this area, methods for determining market prices, for taxation of transactions between interdependent persons, and the procedure for concluding pricing agreements [6]. This definition reflects many aspects of the system for tax control of

transfer pricing, but does not specify how to exercise control functions by tax authorities.

I. V. Manohina and E. V. Yadrennikova noted that tax control of transfer pricing consists in effectively counteracting the use of transfer prices in transactions carried out for the purpose of evading taxes and withdrawing capital abroad by transferring the tax burden to taxpayers with the most favorable taxation

regime or created specifically to accumulate arrears to the budget [7]. Such a definition reveals again the characteristic features of the tax control of transfer pricing, but does not pay attention to the systemacity principle.

In a systematic way, scholars' approaches to the scientific definition of the term "tax control of transfer pricing" are presented in Table 1.1.1.

Table 1. Scientific Approaches to the Definition of the term "Tax Control of Transfer Pricing"

| Authors)                            | Definition of the term "tax control of transfer pricing"   |
|-------------------------------------|--|
| 1                                   | 2  |
| L. F. Sultanova, R. I. Bagautdinova | Activity of state bodies, which consists in the receipt by the state of adequate amounts of taxes that are associated with the application of market prices  |
| N. M. Izmailov, A. V. Soldatenko    | One of the key areas for activity of the tax authorities, which involves counteraction to the use of transfer prices, to evading taxes and to withdrawal of profits from the Russian Federation  |
| L. P. Grundel                       | One of the important directions of the state tax policy, the purpose of which is to ensure counteraction to the use of transfer prices by interdependent organizations in order to minimize taxes  |
| V.A. Shapovalov                     | The activity that involves ensuring fair market pricing by clarifying the list of interdependent persons, controlled transactions, the development of tax control mechanisms in this area, methods for determining market prices, taxation of transactions between interdependent persons, and the procedure for concluding pricing agreements |
| I. V. Manohina, E. V. Yadrennikova  | Effective counteraction to the use of transfer prices in transactions made for the purposes of tax evasion and withdrawal of capital abroad by transferring the tax burden to taxpayers having the most favorable taxation regime or created specifically to accumulate arrears to the budget  |

The following main tasks of tax control transactions between interdependent persons can be called [8]:

- Prevention of export of profits outside the Russian Federation;
- Equitable distribution of tax payments between constituent entities of the Russian Federation by preventing unreasonable transfer of profits to entities with a more favorable level of taxation;
- Harmonization of the tax system of the Russian Federation with international requirements and standards.

Until 2012, the tax control of transactions between interdependent persons was carried out by the norms of Articles 20 and 40 of the Tax Code of the Russian Federation, which were in force since the adoption of part one of the Tax Code of the Russian Federation in 1999. However, already in the early 2000's the ineffectiveness of such control became obvious, what is explained by a number of reasons such as [9]:

- Incompatibility with the norms of international law, in particular with the recommendations of the Organization for Economic Cooperation and Development of 1995, which significantly complicated the activities of large integrated structures, often led to disputes with tax authorities of other countries of the world and double taxation of assets of organizations;

- "Blurring" of the criteria for determining the interdependence of persons, complicating the activities of the tax authorities themselves in the part of proving the illegality of the transactions;

- The lack of the ability to monitor single transactions between persons who are not interdependent on the domestic market of the Russian Federation;

- The absence of a list of official sources of information authorized for use by the police (as a result of different interpretations of the norms from the Tax Code of the Russian Federation, the judiciary took both the side of tax authorities and the side of the taxpayer when considering relevant cases in comparable situations).

These reasons led to a change in the norms of the Tax Code of the Russian Federation and the adoption of the Federal Law dated July 18, 2011 No. 227-FZ "On Amending Certain Legislative Acts of the Russian Federation in Connection with Improving the Principles of Determining Prices for Tax Purposes" [10].

If prior to the adoption of this Law, the problems of tax control between related parties were regulated only by Article 20 and Article 40 of the Tax Code of the Russian Federation, then today there is a whole section (section

V.1) which includes 6 chapters combining 25 articles of the Tax Code of the Russian Federation [11a].

### **Results and Discussion**

Analysis of the approaches of Russian scientists to the definition of the term "tax control of transfer pricing" allows us to proceed to the definition of the content of the term "tax control of transactions between interdependent persons": this is one of the key areas of the state tax policy, which consists in obtaining adequate amounts of taxes by the state, preventing evasion from payment tax and the withdrawal of capital abroad (in low-tax jurisdictions) by clarifying the list of interdependent persons, controlled transactions, tax control of transactions between interdependent persons, methods for determining market prices as well as the procedure for concluding pricing agreements.

Analysis of changes in legislation makes it possible to conclude that the tax control of transactions between interdependent persons has undergone significant changes:

- a) The notion of a "controlled transaction" has been expanded; since 2012, the defining feature of a controlled transaction is the definition of interdependence between persons, and not only certain types of transactions (foreign economic, barter);
- b) The grounds for recognizing persons as interdependent have been significantly expanded, 11 criteria of interdependence between persons are provided except for the share of participation in other organizations;
- c) Change in the basis for the recognition of a price as the market one: since 2012, market prices are those which occurred in transactions between persons who are not interdependent;
- d) The number of methods for determining the market price has been increased; two methods for determining the market price have been added to the existing 3 methods since 2012: the method of comparable profitability and the method of profit distribution;
- e) The list of information sources that the tax authorities can follow when verifying transaction prices has been significantly expanded;
- f) Since 2012, the burden of proof lies on the taxpayer, not the tax authority;
- g) The closed list of taxes that can be subject to adjustment due to inspection of transaction prices by the tax authority is defined concretely;
- h) The right of tax authorities to carry out symmetrical adjustments both for taxpayers and their counterparties, in case of revealing violations during the verification of the reasonableness of the use by individuals of prices in transactions is established;
- i) To achieve stability of pricing, taxpayers are provided with a mechanism to conclude pricing agreements with the tax authority;
- j) A special form of control in the part of tax control in transactions between interdependent persons to control over the completeness, timeliness and accuracy of

calculating taxes when making transactions between interdependent persons, is enshrined.

### **Summary**

Thus, the prerequisites for tax control of transactions between interdependent persons by the state are the concentration of production in holdings and transnational corporations, accompanied by the development of its specialization, the transfer of products manufactured at one enterprise, to another enterprise of the same corporation, active application of the transfer pricing mechanism by integrated structures that allows prices on products to be manipulated within holdings and transnational corporations to minimize taxation.

The basic document on the tax control of transactions between interdependent persons is "OECD Recommendations on Tax Control of Transfer Pricing for Transnational Companies and Tax Authorities", 1995. The OECD recommendations also form the basis for tax control of transactions between interdependent persons and in Russia with certain national peculiarities [12].

### **Conclusions**

In scientific practice, the term "tax control of transfer pricing" prevails, and the term "tax control of transactions between interdependent persons" is used only as the title of section V. 1 of the Tax Code of the Russian Federation. In this connection, the authors of the paper proposed the author's definition of the term "tax control of transactions between interdependent persons": this is one of the key areas of the state tax policy, which consists in obtaining adequate amounts of taxes by the state, avoiding tax evasion and capital withdrawal abroad (low-tax jurisdiction) by clarifying the list of interdependent persons, controlled transactions, tax control of transactions between interdependent persons, methods for determining market prices, and of the conclusion of pricing agreements. Also, the authors of the paper made a comparative analysis of changes in the legislative norms regarding the tax control of transactions between interdependent persons until 2013 and after 2013; the most significant changes were revealed.

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