

**THE APPROACH OF THE RUSSIAN FEDERATION
TO SEPARATION OF POWERS IN TAX MATTERS**

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The meaning of legal indeterminacy in tax matters

2.1. Is your domestic tax legislation vague, when defining the tax object, tax subject and/or tax base, leaving a large margin for discretion, or, is it, on the contrary, very detailed, avoiding indeterminate concepts?

The RF Tax Code (Part I of the RF Tax Code has been in effect since 1 January 1999) states that in the Russian Federation a tax is deemed to be established only when taxpayers and taxation elements are determined, in particular: 1) tax object; 2) tax base; 3) tax period; 4) tax rate; 5) procedure for tax computation; 6) procedure and time periods of tax payment (Art. 17).

Art. 3 (6) of the RF Tax Code which is treated as that which secures one of the principles of tax law states: “when establishing a tax all the elements of taxation should be determined. Legislation on taxes and charges should be formulated in such a way that everyone knows exactly what kinds of taxes (charges), when and in what order he/she will have to pay”.

This rule and many other provisions of the RF Tax Code show explicitly that the Russian legislator proceeds from the intention to clearly and comprehensively regulate tax relations directly by law (statute), and namely – by the RF Tax Code which is adopted as a federal law (statute) and is obligatory on the whole territory of the Russian Federation.

Developing these provisions further Art. 4 of the RF Tax Code limits significantly the powers of executive bodies in taxation. In particular, these limitations can be seen in the following:

- 1) tax bodies do not possess powers to adopt any legal normative acts in the field of taxation, even interpretations which they issue are usually connected with the request of a certain taxpayer and as such are not intended for other taxpayers;
- 2) The RF Government and the RF Ministry of Finance can produce legal normative acts in taxation when it is provided for by a federal law, but they should not change or amend the RF Tax Code. Usually, these acts are adopted as the result of delegated powers to legislate. The acts of these executive bodies (even in the case of delegation) cannot concern the establishment of tax subjects, the objects of taxation, tax bases and other elements of taxation listed in Art. 17 of the RF Tax Code.

The case law of the RF Constitutional Court (since 1995) which started to appear even before adopting the RF Tax Code makes great demands on the determinacy of tax legislation (see Section 2.4).

However, the statutory regulation does not appear that comprehensive in terms of some aspects of establishing *tax base*. A typical example here is the rule concerning the deduction of expenses from the tax base with the purpose of computing the tax on profit of organizations (corporate tax). Along with the

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detailed legislative regulation in Chapter 25 of the RF Tax Code, Art.252 provides also for general principles of recognizing the expenses as those for taxation purposes:

- 1) their economic justification;
- 2) confirmation by documents;
- 3) clear connection with the income (profit) received;

It does not appear possible to give a detailed explanation of these principles directly in the statute – the RF Tax Code. In this case the interpretation of these principles is made by Courts and the case law on the disputes in this sphere is of great significance for the effective application of tax law.

2.2.How do you/does the literature in your country evaluate the use of both techniques in tax legislation?

Academic literature and practical commentaries on tax matters are actually unanimous about the necessity of most detailed legal (statutory) regulation of tax matters, especially of the essential elements of taxation (including the tax object and tax base) directly by the RF Tax Code. On the whole, the negative attitude to the practice of rule-making by tax authorities prevails.

Experts proceed from the idea that the powers to establish a tax and its normative regulation, *on the one hand*, and the powers to collect a tax, *on the other hand*, should be separated. Their combination can lead to the excessive concentration of tax powers and possible abuse. Besides, tax authorities can often change their interpretations of a tax law, usually giving priority to the replenishment of the budget, that's why their regulation is often perceived as legally unreliable and not quite stable.

For this reason, the legislator eventually deprived tax bodies, in principle, of rule-making powers in taxation (Art. 2, 3 and 4 of the RF Tax Code). They can only approve of some forms of tax declarations and reports and also give opinions at individual taxpayers' requests concerning the interpretation of a tax law, exercise tax control, hold inspections of taxpayers and so on.

2.3.Are there independent domestic Courts obliged to control the constitutionality of tax legislation?

In the Russian Federation there are three Courts of High instance:

- 1) The RF Supreme Arbitration Court is in charge of Courts which handle disputes between organizations, businessmen including the disputes of these subjects with tax authorities;
- 2) The RF Supreme Court is in charge of Courts of general jurisdiction, they handle cases between individuals, including their disputes with tax authorities;
- 3) The RF Constitutional Court handles cases concerning the contradictions of certain legal normative acts to the RF Constitution, including the cases on the consistency of federal tax laws, the RF Government rulings on

tax matters, the laws of the RF Subjects (Regions) on taxes with the RF Constitution.

All the three Courts are independent and different from each other in their jurisdiction. The issues of the consistency of a law with the RF Constitution can only be verified by the RF Constitutional Court. Other Courts can, in the framework of their jurisdiction, verify the consistency of an inferior legal normative act with the superior one (except for the cases when this superior act is the RF Constitution).

For example, the RF Supreme Arbitration Court can override the RF Government ruling or an order of the RF Ministry of Finance on tax matters having found them inconsistent with the RF Tax Code. But it is only the RF Constitutional Court who can evaluate the constitutionality of a normative act, for example, recognize some provision of the RF Tax Code inconsistent with the RF Constitution and that's why not subject to application.

2.4. Is legal indeterminacy considered to be unconstitutional/ has a tax rule ever been declared unconstitutional due to legal indeterminacy?

The principle of certainty and preciseness of a tax statute (legislative act) is considered to be one of the principles of tax law which is of constitutional significance. There are far from few examples when the RF Constitutional Court found a legislative act on taxes to be inconsistent with the RF Constitution and not subject to future application because of the indeterminacy of its certain provisions.

But, as a rule, such a violation was identified in connection with the violations of other constitutional principles. For example, if a legislative body (federal or regional) while establishing a tax does not secure sufficient certainty of its legal regime and delegates the detailed elaboration to the executive bodies we can clearly see the violation of at least two principles of the RF Constitution. *Firstly*, the legislative body violates the principle of certainty of tax law and *secondly*, the executive body exceeds its competence if it tries to fill in the lacuna of the legislative regulation and to determine the legal regime of the elements of taxation (including the tax object and tax base) by its normative acts.

If a legislative body while establishing the elements of taxation uses uncertain and ambiguous concepts which allow arbitrary interpretations several constitutional principles are violated.

Firstly, the principle of certainty of taxation (Art. 3 of RF Tax Code) as such is interfered with because the situation creates inadmissible legal indeterminacy in tax relations which will impede normal economic activity.

Secondly, an inadmissible threat is created for the protected legal regime in regard to the taxpayer's property as he/she can actually be arbitrarily deprived of his/her property if a vague tax law is interpreted unfavorably for him/her (Art. 34, 35 of the RF Constitution).

Thirdly, the principle of equality in taxation is also violated, as a vague tax law cannot secure the uniformity of its application practice: it can be applied more favorably in regard to some taxpayers and less favorably – in regard to others. This is a severe violation of the basic constitutional rules which is

relevant not only for tax law but for other branches of the domestic legal system as well.

One of the good examples when a tax rule was recognized to be unconstitutional due to its indeterminacy is the Decision of the RF Constitutional Court of 30 January 2001 No2-P on the case of verifying the constitutionality of Art.20 (1 and 3) of the RF Law “On the fundamentals of the tax system in the RF” and also the Laws on the sales tax of several RF Regions (Chuvash republic, Kirov region and Chelyabinsk region)¹. On the basis of this Decision the sales tax which was introduced by the Laws of the RF Regions according to the Federal law was found to be unconstitutional. One of the key grounds justifying the decision was the insufficient fullness and certainty of the Law which makes the recognition of a person as taxpayer depend on the form of payment for the goods sold. Art. 19 (1), 55 (3) and 57 of the RF Constitution were deemed to have been violated here.

In some cases the RF Constitutional Court having recognized the indeterminacy of a tax law norm can still not recognize it as unconstitutional but give it a clarifying interpretation which follows from the *general sense* of the RF Constitution and the constitutional functions of the norm being challenged. This kind of practice has been expanding recently. As an example we can mention the RF Constitutional Court Decision of 14 July 2003 No12-P on verifying the constitutionality of Art.4, 164 (1), 165 (1 and 4) of the RF Tax Code, Art.11 of the RF Customs Code, Art.10 of the RF Law “On the VAT”². The case concerned the indeterminacy of the tax law norm which regulates what kind of documents can confirm the export of goods beyond the RF customs territory with the purpose of applying the 0% rate of VAT which is imposed in Russia

The consequences of legal indeterminacy in tax matters

3.1. In case of legal indeterminacy not considered to be unconstitutional, who has the final word regarding the interpretation of the rule – the tax authorities or the domestic Courts?

If the legal indeterminacy of a tax law is recognized by the RF Constitutional Court as violating the RF Constitution the law in question is deemed to be unconstitutional and not subject to application.

If the indeterminacy of a tax law is not challenged in respect to the possible violation of fundamental rights and freedoms the application of the law is carried out in the usual order. It is the RF Ministry of Finance who can form the application practice of a tax law clarifying its meaning at the requests of certain taxpayers and on its own initiative. Tax authorities (the Federal Tax Service) possess the same powers but they should coordinate their position with the existing interpretations of the RF Ministry of Finance.

But the interpretations of the RF Ministry of Finance and the Federal Tax Service are only binding for their territorial subdivisions; neither taxpayers nor courts are obliged to be guided by them. As practice shows taxpayers always

¹ The Bulletin (Vestnik) of the RF Constitutional Court, 2001, No3.

² The Bulletin (Vestnik) of the RF Constitutional Court, 2003, No5.

challenge the decisions of tax authorities based on the application of a vague tax law if they disagree with the interpretation offered by tax authorities but the final word belongs to the Courts. Thus, State arbitration courts and Courts of general jurisdiction (taking into account the rules concerning their jurisdiction) develop the interpretation practice of a vague tax norm.

It is worth noting that later a taxpayer can challenge the constitutionality of a vague tax law norm in the RF Constitutional Court not only as it is but also taking into account the meaning of the norm under discussion which has developed in court practice in the course of its interpretation. There were precedents when the RF Constitutional Court having recognized a vague tax norm as constitutional on the whole gave it a proper interpretation in the light of the RF Constitution. Such a new interpretation in fact corrected the already developed practice of some Courts and tax authorities and was binding due to the rules of the Federal constitutional law “On the RF Constitutional Court”.

3.2. Is there a constitutional basis for either the tax authorities or the domestic Courts having the final word on interpretation of indeterminate legal rules?

There is a constitutional basis which determines the legal status of Courts and their functions, in particular in interpreting laws. However, there are no rules of this kind specifically for tax law.

Besides, the positions of the RF Supreme Arbitration Court and the RF Supreme Court, taken in connection with the dispute of tax authorities and a particular taxpayer do not have the nature of a precedent. In principle, tax authorities can go on insisting on the previous interpretation of this category of cases in disputes with other taxpayers, hoping to reverse the practice to their benefit and find new arguments. But if the practice becomes certain enough it often happens that tax authorities begin to be guided by it because of the futility of disputes.

However, from the constitutional law perspective, tax norm interpretations given by the above-mentioned Courts within the framework of certain cases remain unbinding for tax authorities. In this case the principle of separation of powers – judicial and executive – operates.

The situation is different when the interpretation of an indeterminate tax norm is given by the RF Constitutional Court: as it was mentioned above such interpretation becomes binding for all other Courts and executive bodies including the Federal Tax Service and the RF Ministry of Finance. Moreover, even the legislator has to take into account such interpretations and cannot ignore them in the course of their future legislative decisions.

3.3. Is legal indeterminacy normally fulfilled by regulations, administrative rulings and/or case law?

As it was pointed out in the previous section, the legal indeterminacy is fulfilled by case-law. Sometimes, the legislator himself having received the information about the numerous court disputes concerning the content of a particular tax law norm can react promptly and make the wording of the law more detailed.

Complicated and indeterminate tax law norms are also fulfilled by different individual interpretations of the RF Ministry of Finance and tax authorities at the requests of individual taxpayers. It happens quite often that these interpretations are published by these authorities or put into the professional database of legal documents and in that way they become accessible for a wide range of taxpayers and influence their behavior. However, from the legal perspective they remain unbinding for taxpayers. Getting acquainted with such interpretations taxpayers can be more precise in evaluating whether they will have to be in dispute with tax authorities due to their disagreement with the interpretation given by tax authorities. As a rule, if companies and businessmen disagree with the position of tax authorities, they often go to Court taking into account that the proceedings in State arbitration courts are relatively fast (6-9 months for all three instances: the first, appeal and cassation).

3.4. Are administrative rulings binding to the taxpayer and/or the Courts?

As it has been mentioned above the rulings and recommendations of the Federal Tax Service and the RF Ministry of Finance are not binding for taxpayers and Courts as, according to the general rule, are considered to be neither *normative acts* nor *individual enforcement acts* obligatory for execution. They are seen only as *opinions* of these authorities. In particular, Courts examine them along with the evidence and facts of the case. However, such rulings and recommendations are binding for all territorial tax authorities in the order of administrative subordination (RF Law “On tax authorities”, Art. 30 of the RF Tax Code).

In some cases the RF Ministry of Finance due to Art.4 (1) of the RF Tax Code can give the form of normative legal act to their rulings. This happens quite seldom because of the general ban on any changes and amendments of tax legislation by acts of executive bodies. However, if any grounds are found in a law (statute) for the RF Ministry of Finance to adopt such a tax ruling, it will become binding for taxpayers and Courts after its official publication and registration at the RF Ministry of Justice. But Courts (we mean State arbitration courts and Court of general jurisdictions of any instance) may not apply it in a certain case if they consider that this ruling of the RF Ministry of Finance contradicts a tax legislative act (or another superior normative act) or that the RF Ministry of Finance exceeded its authority by adopting this act.

Relationship between the Tax Administration and the Domestic Tax Courts:

4.1. Do your domestic Courts control application of tax law by your Tax Administration?

Courts of general jurisdiction and State arbitration courts (with the account of the established rules on their jurisdiction) have full control over the application of tax law norms by tax authorities. However, the control can usually be initiated by a taxpayer or another subject who thinks that the decisions (actions) of a tax body

have violated his/her rights. According to Art.137-138 of the RF Tax Code these taxpayers can challenge any actions and decisions of a tax body and its officials if they can prove that these actions and decisions violate their legal rights and interests. The complaint can be made in accordance with the RF Civil Procedure Code or the RF Arbitration Procedure Code depending on what kind of Court a taxpayer can go to.

According to the general rules (Chapters 19 and 20 of the RF Tax Code) the taxpayer can go to Court straight away without trying to settle the dispute with Tax Administration. As an exception, Art.102.2 of the RF Tax Code provides that the decision of a tax body to impose sanction on a taxpayer should first be challenged in the superior tax body and only then, if the taxpayer is still dissatisfied with the decision – in the Court (in the usual order).

Besides, there are many cases when Courts exercise preliminary judicial control, for example, Tax Administration can collect a tax debt of an individual (a natural person) only applying to the Court and on the basis of Court decision.

4.2. Do your domestic Courts, in their case law, take into account rulings and binding information emerging from your Tax Administration?

As has been mentioned above, Courts take into account rulings (recommendations) and other information from the Federal Tax Service only as other facts of the case. Such rulings and recommendations are not legally binding for them. However, Art.111 (1 and 3) of the RF Tax Code contains an important exception. If it is found that a taxpayer followed an official ruling or recommendation of the Tax Administration or the RF Ministry of Finance and this ruling (recommendation) was found wrong, from the Court's perspective, the taxpayer cannot be subject to any penalties or sanctions in connection with the respective violation of a tax law (in its correct interpretation). But in this case we deal with the special legal guarantees for taxpayers and not with special powers of tax bodies.

4.3. Does your Tax Administration take into account the domestic courts case law and/or the ECJ case law when applying the law?

Summing up the above-mentioned we can point out the following directions of the influence of case law:

- 1) The Federal Tax Service has always to apply and take into account in its activities the decisions of the RF Constitutional Court;
- 2) The case law of State arbitration courts and Courts of general jurisdiction is not legally binding for Tax Administration, but in fact, they have to monitor it closely and take into account otherwise any its decision which contradicts this case law can be overridden if a taxpayer goes to Court. There are situations when the Federal Tax Service sends out State arbitration court decisions on the recent cases (in spite of the fact that most of such materials are available for general public) in order to attract the attention of territorial tax bodies to the changes in case law.

The Federal Tax Service of the Russian Federation as that of a Non-member EU State is not guided by the case law of the ECJ. The ECJ case law can be

studied in regard to some complicated cases as examples of decisions on similar cases in foreign law.

4.4. Is there a principle of reciprocal observation of the interpretation of tax law by the Tax Administration and domestic Courts?

The principle of reciprocal observation of the interpretation of tax law is not established by the RF legislation.

Occasionally we can even come across certain deviations in the interpretation of tax laws by different Courts: the RF Constitutional Court, the RF Supreme Court, the RF Supreme Arbitration Court. These deviations are not of system character, though.

In case of divergence in the interpretation of a tax norm between Courts and the Federal Tax Administration the latter sooner or later will have to step back because, if case law is quite unanimous, each decision of any tax body which contradicts the interpretation developed by Courts will be found invalid (though a taxpayer will have to initiate the court procedure). Moreover, a taxpayer can lay claim to the compensation of court expenses by Tax Administration.

In practice, however, the interpretation of many indeterminate tax norms (e.g. Art.252 of the RF Tax Code) depends on different individual facts of a certain case which leads to divergence in case law. In such conditions a tax body can make reference to the case law which is more favorable for its position in regard to the disputable tax norm.

4.5. Is your Tax Administration legally bound to the decisions of supreme courts and/or the ECJ?

The Tax Administration will be legally bound by the decisions given by the RF Constitutional Court in regard to the legal position in interpreting a certain tax law norm. If the RF Constitutional Court recognizes a certain norm as unconstitutional it becomes invalid and such a decision is also binding for any state authorities and other subjects.

The decisions of other RF superior courts are only binding for the Tax Administration within the framework of the case on which they were made. They do not acquire the nature of a precedent. The decisions of the ECJ are not binding as the Russian Federation has no status of an EU Member State.

4.6. Does your Tax Administration circumvent your domestic courts' case law?

As a rule, any indeterminate tax law norm results in divergence of its application practice which can be divided into groups with the account of typical facts which can influence its interpretation.

In any category of cases if the Tax Administration disagrees with the developed case law interpretation, it tries to give new arguments (justification) in the further cases of this category in order to form a new and more favorable direction in court practice.

As an example we can mention the disputes concerning the interpretation of Art.172 of the RF Tax Code which regulates the right for VAT deductions. The disputes were connected with the possibility of deducting the VAT sums, which have previously been paid as a part of goods price to the company which in fact

does not exist or does not actually carry out any economic activities, from the VAT amount due to be transferred into the budget. Over the recent 8 years of this norm being in effect the Tax Administration managed to implement essential corrective actions in regard to case law and persuade Courts to interpret Art.172 more strictly when there are any suspicions of tax fraud.

II

**Please answer the following questionnaire,
which aims at confirming your answers in I**

1. Relationship between the Parliament and the Tax Authorities: The influence of the tax authorities on tax legislation

1.1. Does your Parliament control tax authorities in an efficient way? yes – **no (not directly)**

The Parliament does not exercise any direct control over the Federal Tax Service. However, it controls the RF Government on the whole which is accountable to the Parliament. The RF Government and Courts in their turn control tax authorities.

1.2. Do tax authorities influence tax legislation to a major degree? yes – **no (not directly)**

Tax authorities cannot directly influence tax legislation. However, their proposals can be submitted to the Parliament through the RF Ministry of Finance and the RF Government. In practice, the RF Ministry of Finance can exert significant influence on tax policy and amendments of tax legislation.

1.3. Does your Parliament a) usually accept the bills provided by tax authorities?

Yes (bills proposed by the RF Ministry of Finance) - no

b) refuse the bills provided by tax authorities? never –
sometimes (bills proposed by the RF Ministry of Finance) - often

c) improve the bills provided by tax authorities? never –
sometimes (bills proposed by the RF Ministry of Finance) - often

1.4. Is your Parliament able to discuss the bills thoroughly? **yes - no**

1.5. Is there sufficient knowledge of tax law in Parliament? **yes – no; by not all the members**

Only some members of special parliamentary committees usually have knowledge of tax law.

1.6. Are tax rules often so vague, that tax authorities have to fill the gaps themselves by administrative regulations? **Never (almost never)** - sometimes - often

1.7. Have tax authorities the competence to typify and fill out the legal gaps without control by the Parliament? **never** - sometimes - often

2. Relationship between the Parliament and the Domestic Tax Courts

2.1. Are there independent (Tax) Courts in your country entitled to control legislation?

There is no special Tax Court in the Russian Federation, however, judges of State arbitration courts usually specialize in particular categories of cases (e.g. tax cases) and, to some extent, the same can be seen in other courts. In principle, Courts have sufficient powers to control legislation.

2.2. If “yes”, do they control tax legislation: 0 ex ante or 0 ex post?
Ex post

2.3. Are Courts competent to clarify whether a specific written tax rule is compatible with constitutional standards? **yes** - no

2.4. If a high Court is convinced that a specific tax law violates constitutional standards, is the court in this case allowed to ignore the law? **Only in some cases**

If a certain tax law violates constitutional standards the RF Constitutional Court has to recognize it as unconstitutional and by this cease its effect on the whole RF territory.

If State arbitration courts or Courts of general jurisdiction dealing with a particular case think that the federal law (statute) which is due to be applied in this case, violates the RF Constitution they have to suspend the case and forward a request to the RF Constitutional Court. A taxpayer is also entitled to forward such a request (complaint) if his/her rights are violated by an unconstitutional, in his\her opinion, law in the framework of a particular case.

However, State arbitration courts and Courts of general jurisdiction cannot ignore (before a positive RF Constitutional Court decision) a federal law subject to be applied. They can ignore a normative act of a lower legal level (e.g. ruling of the Government, order of the Ministry of Finance and etc.) in a similar situation.

3. Relationship between the Tax Administration and the Domestic Tax Courts

3.1. Are there independent (Tax) Courts in your country, obliged to control your Tax Administration?

Independent Courts have to control Tax Administration usually at taxpayers' requests. Besides, when collecting tax debts from an individual (a natural person) or collecting substantial tax fines from any taxpayers and in some other cases Courts exercise preliminary judicial control, that is a tax body will have to address a Court in order to make a collection (Art.48 of the RF Tax Code).

3.2. Are your domestic Courts bound to administrative regulations/orders/rulings, which are issued by tax authorities? yes - **no**

If "no", do the courts follow them in fact? never - **sometimes** – often - very often

3.3. Are first instance Court decisions on a tax case, normally accepted by the Tax Administration (i.e. do they not try to appeal against the decision)? never – **sometimes (They are usually accepted when a decision is at least partly in favor of the Tax Administration)** - often - very often

According to the “inside” regulations tax authorities have to use all remedies (appeal or (and) cassation complaint) if the position of Tax Administration is not supported)

3.4. Is a final judicial decision on a single tax case, followed by the Tax Administration not only in this case but also in all other similar cases? never - **sometimes** - often - very often

3.5. How does the Tax Administration react when it is convinced that the final judicial decision is wrong or not "acceptable" because, e.g., it is too expensive for the public?

a) Does it accept the (from their point of view) wrong decision? Never (**almost never or only if all possibilities for complaining were completely used**) - sometimes - often - very often

b) Does it try in another similar case to convince the Court to decide in a different way? never - sometimes - often - **very often**

c) Does it try to influence the Parliament to change the law? never - **sometimes** - often - very often

d) Does it make sure that the Internal Revenue Service will not follow this decision in similar cases? never - sometimes - often - **very often**

e) Does it try “to hide” such a decision, e.g., not publishing the decision with the result that the Internal Revenue Service does not know this decision? **Never (at least, there is no such information)** - sometimes - often - very often