transfer pricing legislation

In accordance with the Work Plan of the Supreme Court of the Republic of Kazakhstan for the second half of 2018, a generalization of judicial practice in the application of transfer pricing legislation was carried out.

The purpose of the generalization is to study judicial practice in cases of the generalized category, analyze the quality of the administration of justice, develop proposals for the formation of a uniform application of legislation, and identify problematic issues that arise in the law enforcement practice of courts.

The generalization was carried out for the period 2015-2017 and the 1st half of 2018, based on the study and analysis of 18 civil cases, judicial acts included in the Information System "Torelik" on cases of the generalized category, certificates on the results of generalizations carried out by regional and equated courts (hereinafter referred to as regional courts), as well as the practices of the specialized judicial collegium and the collegium for civil cases of the Supreme Court.

Legal framework:

The main regulatory legal acts that courts should be guided by when considering cases related to the application of transfer pricing legislation are: - The Constitution of the Republic of Kazakhstan;

- Law of the Republic of Kazakhstan dated July 5, 2008 "On transfer pricing";

- Code of the Republic of Kazakhstan "On taxes and other obligatory payments to the budget (Tax Code)";

- Entrepreneurial Code of the Republic of Kazakhstan (hereinafter - PC); - Civil Procedure Code of the Republic of Kazakhstan (hereinafter referred to as CPC);

- Civil Code of the Republic of Kazakhstan (hereinafter referred to as the Civil Code); - Decrees of the Government of the Republic of Kazakhstan:

1. "On the conclusion of the Protocol on the exchange of information on control over transfer pricing between the tax and customs authorities of the Member States of the Eurasian Economic Community" dated March 23, 2005 No. 259;

2. "On approval of the List of officially recognized sources of information on market prices" dated March 12, 2009 No. 292 (as amended on December 30, 2009, January 16, 2012, July 17, 2018);

3. “On approval of the List of goods (works, services), international business transactions for which are subject to transaction monitoring” dated March 12, 2009 No. 293 (lost force by the Decree of the Government of the Republic of Kazakhstan dated August 28, 2015 No. 685);

4. “On Approval of the List of Exchange Commodities” dated May 6, 2009 No. 638 (as amended on January 16, 2012);

- orders of the Minister of Finance of the Republic of Kazakhstan:

1. “On Approval of the Rules for Monitoring Transactions” dated March 16, 2015 No. 176;

2. “On Approval of the List of Goods (Works, Services), International Business Transactions for Which Are Subject to Transactions Monitoring” dated March 19, 2015 No. 194;

3. “On approval of cross-country reporting forms and an application for participation in an international group and the Rules for filling them out” dated February 14, 2018 No. 178;

- normative resolutions of the Supreme Court of the Republic of Kazakhstan:

1. "On judicial practice in the application of tax legislation" dated June 29, 2017 No. 4;

2. “On some issues of application by courts of the norms of Chapter 29 of the Civil Procedure Code of the Republic of Kazakhstan” dated December 24, 2010 No. 20;

3. “On the Judgment” dated July 5, 2003 No. 5.

Analysis of transfer pricing legislation

For the first time, transfer pricing issues were enshrined at the legislative level in the 60s of the last century in the United States. In Kazakhstan, these issues began to be regulated with the adoption of the Decree of the President of the Republic of Kazakhstan, having the force of law, dated April 24, 1995 No. 2235 “On taxes and other obligatory payments to the budget” (hereinafter referred to as the Decree on taxes).

Moreover, only one article - 138. According to paragraph 6 of this article, if a taxpayer applies prices in its commercial or financial transactions with a related party that differ from those applied between independent enterprises, then for tax purposes the tax service adjusts the taxpayer's income for the resulting difference in prices, if one of the parties is a non-resident of the Republic of Kazakhstan or an organization enjoying tax benefits. At conducting such transactions, the tax service may reclassify these transactions in order to determine their real nature and impose penalties.

*By the Law of the Republic of Kazakhstan dated December 28, 1998, the above paragraph was excluded and the Tax Decree was supplemented by Article 138-1.*In this article, consisting of 15 points, the legislator provided for the right of tax authorities to control the correctness of applying prices for transactions:

1) between related parties;

2) on commodity exchange (barter) transactions;

3) with a significant fluctuation (more than 20 percent in one direction or another) in the price level applied by the taxpayer for identical (homogeneous) goods (works, services) within a quarter.

At the same time, the provisions of Article 138-1 of the Decree on Taxes applied both to transactions made by business entities within Kazakhstan and to transactions made in the course of international commercial transactions.

The usual method for determining the market price of goods and services was to apply comparable terms of transactions between unrelated parties.

In the absence of transactions on a particular market for identical (homogeneous) goods (works, services) or due to the lack of supply of such goods (works, services) on this market, as well as when it is impossible to determine the corresponding prices due to the absence or unavailability of information sources for determining the market prices could use the following methods:

1) resale price method;

2) cost method.

Law of the Republic of Kazakhstan dated January 5, 2001 "On state control in the application of transfer prices"(hereinafter referred to as the Law on State Control over the Application of Transfer Prices) established measures of state control over the application of transfer prices in order to prevent the loss of state income in international business transactions. This Law consisted of 13 articles.

In connection with the enactment of a special law, Article 138-1 of the Decree on Taxes became invalid, and Article 138 was amended to refer to this law.

Thus, with the adoption of the Law on State Control over the Application of Transfer Pricing, the transfer pricing legislation was finalized.

Tax legislation after the exclusion from it of substantive rules governing the implementation of state control over the application of transfer pricing, retained only the rules on the procedure for appointing and conducting thematic audits on transfer pricing issues.

Paragraph 2 of Article 3 of the Law on State Control, when applying transfer prices, provided that state control is exercised on the following transactions:

1) between interdependent or related parties;

2) on commodity exchange (barter) transactions;

3) when fulfilling obligations under transactions carried out by way of set-off (counter homogeneous claim, including set-off upon assignment of a claim);

4) when making transactions with persons registered (residing) or having bank accounts in foreign countries, the legislation of which does not provide for the disclosure and provision of information in the course of financial transactions or at the place of registration (residence) of which a preferential taxation regime is applied, including offshore zones;

5) when making transactions with legal entities that have tax benefits or for which a rate is set that is different from the rate established by tax legislation;

6) when making transactions with legal entities that have a loss according to tax returns for the last two tax periods preceding the year in which the transaction was made.

In addition, for international business transactions that are not subject to paragraphs 1-6 of this paragraph, state control is carried out if the fact of the transaction price deviating by more than 10 percent in one direction or another from the market price is established. For transactions carried out on the territory of the Republic of Kazakhstan and subject to paragraphs 5 and 6, state control is exercised in case of their relationship with international business transactions.

Consequently, the adopted special law provided for the implementation of state control not only over international business transactions, but also over transactions

made on the territory of the Republic of Kazakhstan, provided that they are interconnected with international business transactions.

In accordance with the Law, the tax authorities used the following methods to determine the market price:

- comparable uncontrolled price method;

- cost plus method;

- the method of the price of subsequent sale (resale).

The Law on State Control in the application of transfer prices recognizes the possibility of the existence of certain conditions, affecting price fluctuations. Their presence did not entail the adjustment of objects of taxation. They included, inter alia:
1) the volume of delivered goods, performed works or rendered services;

2) seasonal fluctuations;

3) differences in the quality of goods sold and other purchasing characteristics;

4) marketing policy for promoting new products on the market;

5) samples and trial specimens;

6) payment terms;

7) deadlines for the fulfillment of obligations.

Article 9 of the Law on State Control, when applying transfer prices, established the sources of information used to determine the market price: officially recognized sources and information provided by participants in transactions.

Since January 1, 2009, the Law of the Republic of Kazakhstan dated July 5, 2008 "On Transfer Pricing" (hereinafter – the Law on Transfer Pricing) has been in force in the country.

This law takes into account international principles and standards for control over transfer pricing (Organization for Economic Co-operation and Development (OECD) Guidelines on Transfer Pricing for Multinational Corporations and Tax Administrations, 1995).

The current legislation on transfer pricing regulates public relations arising from transfer pricing in order to prevent the loss of state income in international business transactions and transactions related to international business transactions.

According to the definition given in subparagraph 25) of Article 2 of the Transfer Pricing Law, the transfer price is recognized as the price that exists in transactions not only between related parties, but also differs from the market price.

Thus, the legislator established the possibility of exercising control in transfer pricing not only between related parties, but also between independent parties.

By virtue of Article 3 of the Transfer Pricing Law, control over transfer pricing is carried out on international business transactions (export, import of goods) and transactions made on the territory of the Republic of Kazakhstan, directly related to international business transactions:

- for minerals mined by a subsoil user that is one of the parties;

- one of the parties of which has tax benefits;

- one of the parties of which has a loss according to tax returns for the last two tax periods preceding the year of the transaction.

The Law on Transfer Pricing introduced reporting on transaction monitoring and transfer pricing, introduced the concept of a price range, and the rule of deviation of the transaction price from the market price by more than 10% was retained only for transactions with agricultural products.

If during the audit a deviation of the transaction price from the market price is established *adjustment of the object of taxation is made taking into account the range of prices*. Price range - a range of market price values, limited by the minimum and maximum values of market prices, determined as a result of applying one of the methods for determining market prices or sources of information in the manner prescribed by the Transfer Pricing Law.

Adjustment of objects of taxation is made when the transaction price deviates from the market price as an average value specified in the source of information on the participants in the transaction:

1) registered in a state with preferential taxation;

2) carrying out commodity exchange (barter) operations;

3) having a loss according to tax returns for the two last tax period preceding the year of the transaction;

4) having tax benefits;

5) carrying out the fulfillment of obligations under transactions made by offsetting a counter homogeneous claim (including offsetting upon assignment of a claim).

In Article 12 of the Law on Transfer Pricing, the methods for determining the market price are increased to 5. In addition to the previously mentioned, methods for distributing profits and net profit are indicated.

If it is impossible to apply the comparable uncontrolled price method, one of the methods specified in paragraph 1 of Article 12 shall be successively applied.

Therefore, if the tax authorities apply the 2nd and subsequent methods during audits, the audit report must contain an indication that it is impossible to apply the previous method.

Article 18 of the Law on Transfer Pricing establishes the order of application of sources of information used to determine the market price:

1) officially recognized sources of information on market prices;

2) sources of information about stock quotes;

3) data of state bodies, authorized bodies of other states and organizations on prices, differential, expenses and on conditions affecting the deviation of the transaction price from the market price;

4) information programs used for transfer pricing purposes, information provided by participants in transactions, and other sources of information.

In a transaction, the participant of which is registered in a state with preferential taxation, when determining the market price, only the sources of information specified in subparagraphs 1) and 2) of paragraph 1 of this article are used.

Incoterms- On January 1, 2011, the edition of Incoterms 2010 came into force, which applies not only to international, but also to domestic trade.

Drawing up and concluding contracts for the supply of goods requires the parties to know special terminology. In order to avoid cases of misinterpretation of the concepts used in the field of foreign economic activity and, as a result, the occurrence of disputes, it is necessary to be guided by the rules enshrined in Incoterms.

Incoterms— international rules in the form of a dictionary containing a list of terms most widely used in concluding external supply contracts, and exhaustive definitions for them. Its main task is to standardize and optimize the terms of international supply

contracts to bring them into line with the laws of all countries participating in the contract.

Allocation of responsibility according to INCOTERMS 2010

International trade terms are designed to regulate the following areas of trade relations:

• Determining the date of delivery of goods.

• Distribution between the parties to the contract of transport costs and other costs associated with the carriage of goods;

• Settlement of conditions for the transfer of responsibility for the risks associated with the destruction, loss or damage of goods during transportation.

Contents of Incoterms 2010

All terms included in Incoterms are designated as a three-letter abbreviation, the first letter of which indicates the moment and place of transfer of obligations from the supplier to the recipient:

AND- (English departure, shipment). Obligations pass to the buyer directly at the time of dispatch and, accordingly, at the place of dispatch of the goods;

F - (English main carriage unpaid, the main carriage is not paid). The point of transition of obligations is the terminal of departure of the transportation, provided that the main part of the transportation remains unpaid;

C - (English main carriage paid, the main carriage is paid). Payment for the main carriage is made in full, obligations are transferred at the moment the cargo arrives at the arrival terminal;

D - (English arrival, arrival). "Full delivery", when the transfer of obligations is carried out at the time of acceptance of the goods by the buyer. The current terms of delivery of Incoterms 2010 contain 11 terms, of which 7 are applicable to cargo transportation by any mode of transport, and 4 - exclusively to the methods of delivery of goods by water transport (sea transport and transport of territorial waters).

Universal terms:

EXW- (English ex works, ex-warehouse, ex-factory). "Pickup" or category of transportation, where the free point, that is, the place of transfer of responsibility from the supplier to the recipient, is directly the seller's warehouse.

FCA - (English free carrier, free carrier). A regime that obliges the seller to deliver the goods to the place of receipt by the carrier in accordance with the terms of the contract (payment of export duties is the responsibility of the supplier).

CPT - (eng. carriage paid to .., transportation paid to ..). Payment for the main part of the carriage, that is, to the point of arrival, lies with the seller, who, in accordance with the contract, delivers the goods to the carrier (expenses for insurance and customs fees, fees for import and customs clearance on the buyer).

CIP - (eng. carriage and insurance paid to .., transportation and insurance paid to ..). Delivery mode, almost similar to the CPT category, the difference lies in the obligation to pay insurance on the seller.

THAT- (English delivered at terminal, delivery to the terminal). The distribution of costs between the seller and the buyer: the first pays for delivery to the arrival terminal and export payments and insurance fees, the second - customs clearance and the rest of the transportation to the destination.

DAP- (English delivered at place, delivery to the place). Delivery of goods to the destination with the obligation to pay import duties and taxes to the address of the recipient state on the buyer.

DDP - (English delivered duty paid, delivery with payment of duties). Delivery of goods to the destination with the imposition of costs on the seller in full.

Terms applied to cargo transportation, carried out by sea and other water transport:

FOB - (English free on board, free board). Shipment of goods to a vessel owned by the buyer or paid for by him, while paying for part of the delivery to the terminal is the responsibility of the seller.

FAS - (English free alongside ship, freely along the side of the vessel). Delivery of goods to the buyer's ship without shipment. The burden of paying for shipment and delivery lies with the recipient.

CFR - (English cost and freight, cost and freight). Transportation of cargo to the port specified in the contract. All costs for delivery, payment of insurance, unloading and trans-shipment operations are borne by the buyer himself.

CIF - (English cost, insurance and freight, cost, insurance and freight). Delivery mode similar to CFR category, however insurance premiums are the responsibility of the seller.

Quantitative indicators for cases of the generalized category

It should be noted that court reporting forms do not provide for the maintenance of a separate statistical column for disputes arising on transfer pricing issues.

Statistics are presented on the basis of information from regional courts. **In 2015**the number of completed cases of the generalized category is 9 or 0.7% of the total number of completed cases in the republic on challenging decisions and actions (inaction) of tax authorities*(1330).* Considered with decisions 9 cases or 10% of the total number completed with decisions*(900),* 4 of them - about partial satisfaction of applications, 5 - about refusal.

In 2016 courts completed proceedings in 7 cases, which is 2 cases less than in 2015, and accounts for 0.3% of the total number of completed cases on challenging decisions and actions (inaction) of tax authorities*(2543).*

Judgments were made in 7 cases, which is equal to 0.5% of the total number of cases completed with decisions*(1613).* Of these, in 2 cases, applications were satisfied*(1- in full, 1- partially),*in 5 cases - denied.

In 2017 in the republic, proceedings were completed in 7 cases, which is equal to the figures for the past period and forms 0.4% of the total number of completed cases on challenging decisions and actions (inaction) of tax authorities*(2017 section).*

Decisions were made in 7 cases, which is 0.5% of the total number of cases completed with decisions*(1613).* Of these, in 4 cases the applications were partially satisfied, in 3 cases they were denied.

In the first half of 2018, proceedings were completed in 2 cases of the generalized category, which forms 0.3% of the total number of completed cases on challenging decisions and actions (inaction) of the tax authorities*(890).* Decisions were made in 2 cases or 0.4% of the total number of cases completed with the issuance of decisions*(557),* applications are partially satisfied.

Statistical information for the generalized period indicates a gradual decrease in the number of applications received by the courts of the republic in this category of cases.

Information on cases of challenging notifications by year – 2015

1	2	3	4	5	6

№	and etc with a l b about	about l and p in etc with about p about Me is with V	l and n is sh is p m is and n is with is n y V with		from column 4					
					beats V complete volume		beats partially		denied	
					. h and l about To	amounts	. h and l about To	amounts	. h and l about To	amounts
1	Almaty	3	3	5 208 929 973					3	5 208 929 973
2	Akmola	1	1	107 671 114			1	2 164 363		105 506 751
3	Kyzylordin sky	1	1	28 634 764 365			1	5 391 482		28 629 732 883
4	Mangistau sky	3	3	11 781 995 526			1		2	11 771 322 410
5	Pavlodarskaya	1	1	1 363 516 468			1	1 345 910 972		17 605 496
	total	9	9	47 096 877 446			4	1 364 139 933	5	45 733 097 513

For 12 months of 2015, 9 decisions were appealed on appeal*(left unchanged - 7, changed - 2 (Akmola -1, Mangistau -1).*

Judicial acts in 7 cases reviewed in cassation*(left unchanged - 3, changed - 2 (Mangistau -1, Pavlodar -1), canceled - 2 (Almaty - 2).*

Judicial acts in 3 cases reviewed in supervisory order*(changed - 2 (Mangistau -2), canceled - 1 (Mangistau).*

2016 year

1	2	3	4	5	6					
№	and etc with a l b about	about l and p in etc with about p about Mr is with V	l and n is sh is p m is and n is with is n y V with	y m m in with is y m is a V and p a p with about	from column 4					
					beats V complete volume		beats partially		denied	
					. h and l about To	amounts	. h and l about To	amounts	. h and l about To	amounts
1	Astana	1	1	876 600 000					1	876 600 000
2	Almaty	3	3	3 482 997 559	1	3 063 852 934			2	419 144 625
3	Kyzylordinskaya	1	1	19 030 849					1	19 030 849
4	SKO	2	2	179 706 373			1	13 023 047	1	166 686 326

	total	7	7	4 558 334 781	1	3 076 875 981	1	13 023 047	5	1 481 461 800

Case quality in higher authorities

For 12 months of 2016, 7 decisions were appealed on appeal, all were left unchanged.

Based on the results of the cassation review, the considered judicial acts in 2 cases were left unchanged.

2017 year

1	2	3	4	5	6					
№	and etc with a l b about	about l and p in etc with about p about Mr is with V	l and n is sh is p m is and n is with is n y V with	y m m in with is y m is a V and p a p with about	from column 4					
					beats V complete volume		beats partially		denied	
					. h and l about To	amounts	. h and l about To	amounts	. h and l about To	amounts
1	Astana	5	5	15 089 039 795			4	6 926 191 082	1	8 162 848 713
2	SKO	2	2	82 398 530					2	82 398 530
3	total	7	7	15 171 438 325			4	6 926 191 082	3	8 245 247 243

The quality of consideration of cases in higher instances

For 12 months of 2017, 7 decisions were appealed on appeal (left unchanged - 4, changed -3 (Astana).

1st half of 2018

1	2	3	4	5	6					
№	and etc with a l b about	about l and p in etc with about p about Mr is with V	l and n is sh is p m is and n is with is n y V with	y m m in with is y m is a V and p a p with about	from column 4					
					beats V complete volume		beats partially		denied	
					. h and l about To	amounts	. h and l about To	amounts	. h and l about To	amounts
1	Astana	2	2	1 773 000 700			2	527 000 000		1 246 000 700
	total	2	2	1 773 000 700			2	527 000 000		1 246 000 700

From the given statistical data it follows that the largest number of cases of this category was considered by the courts of Astana, Almaty and Mangistau region.

Pre-trial settlement of disputes

The current legislation defines an alternative procedure for resolving disputes about challenging decisions, actions (inaction) of state revenue bodies. The applicant has the right to appeal: notification of the results of the inspection to the authorized body or to the court; actions (inaction) of officials of state revenue bodies to a higher authority or to a court.

Since July 1, 2017, the Appeals Commission has been established by the authorized body - the Ministry of Finance to consider complaints about the notification of the results of the audit.

The authorized body makes a reasoned decision, taking into account the decision of the Appeal Commission.

From the analysis carried out by the authorized body, it follows that in the second half of 2017 it considered 70 complaints, of which 20 were satisfied (notifications were cancelled).

In the first half of this year, 134 complaints were considered, of which 53 or 40% were satisfied. It should be noted that only one percent of the issues appealed by taxpayers relates to transfer pricing.

In the course of studying the cases received for generalization, it was found that in 17 out of 18 taxpayers previously appealed the notifications of the results of the audit out of court.

Jurisdiction

Until January 1, 2016, disputes arising in connection with the exercise of control in transfer pricing were considered by specialized inter-district economic courts.

With the adoption of the Civil Procedure Code of the Republic of Kazakhstan dated October 31, 2015, there have been significant changes in the jurisdiction of this category of cases.

In accordance with part 4 of Article 27 of the Code of Civil Procedure, the court of the city of Astana, according to the rules of the court of first instance, considers civil cases on investment disputes, except for cases within the jurisdiction of the Supreme Court of the Republic of Kazakhstan.

The Astana City Court also considers other disputes between investors and state bodies related to the investor's investment activities.

Other disputes related to investment activities include disputes between an investor and a state body related to violation of the legislation of the Republic of Kazakhstan.

These, among other things, include cases on claims for the recognition of illegal decisions of state bodies on the accrual of tax, customs and other obligatory payments to the budget by investors.

Regardless of the status of the investor (large or small), such cases are under the jurisdiction of the court of the city of Astana.

Questions arose in the courts with the correct definition of the jurisdiction of the case.

Disputes between the investor and state bodies based on relations of power and subordination, which have arisen as a result of the exercise by these bodies of the competence prescribed to them by the state, cannot be classified as investment disputes.

Thus, on October 25, 2017, Company M filed a petition with the Supreme Court challenging the notification of the tax authority based on the results of the audit. The company indicated that it is a major investor and the dispute is an investment one.

The application was accepted for proceedings by the specialized judicial board of the Supreme Court.

However, later the case was sent under jurisdiction to the court of the city of Astana. In the ruling, the court indicated that the dispute is not an investment one, since it does not arise from contractual obligations. Disputes between the investor and state bodies based on relations of power and subordination (for example, disputes with tax, customs, environmental authorities and other bodies) arising from the exercise by these bodies of the competence prescribed by the state cannot be classified as investment. Such non-contractual disputes between the investor and state authorities are referred to the competence of the court of the city of Astana as "other disputes related to investment activities".

Transfer pricing controls

In accordance with paragraph 2 of Article 3 of the Transfer Pricing Law, control is exercised by the authorized bodies:

1) monitoring transactions;

2) checks;

3) other procedures established by the laws of the Republic of Kazakhstan. The generalization showed that in the courts, the notifications issued on the basis of the results of inspections were mainly the subject of consideration. According to Article 9 of the Law on Transfer Pricing, the authorized bodies conduct inspections on transfer pricing issues in the following cases:

4) when determining the deviation of the transaction price from the market price; 2) on the basis of information on the facts of the application of transfer prices received from state bodies;

5) when conducting inspections carried out by authorized bodies on compliance with the tax legislation of the Republic

Kazakhstan and the customs legislation of the Eurasian Economic Union and (or) the Republic of Kazakhstan in the absence of sources of information on market prices.

State control in the field of application of transfer prices is carried out in the form of verification and other forms.

The verification is carried out in accordance with the Entrepreneurial Code of the Republic of Kazakhstan. Other forms of state control are carried out in accordance with this Law.

Features of the procedure and terms for conducting an audit and other forms of state control carried out by state revenue bodies are determined by the tax legislation of the Republic of Kazakhstan and the customs legislation of the Eurasian Economic Union and (or) the Republic of Kazakhstan.

Articles 141, 142 of the current Tax Code provide that a thematic audit can be carried out on transfer pricing issues, and this issue can also be included in a comprehensive audit.

Similar provisions were contained in Article 627 of the 2008 Tax Code.

Liquidation due diligence is complex and may include issues of compliance with transfer pricing legislation.

LLP "K" disputed the legality of the audit on the grounds that the transfer pricing audit was carried out without a prescription for the type of audit.

The courts of the Akmola region found the applicant's arguments unfounded. It was established that the inspection was appointed and carried out on the application for the liquidation of the Partnership. That is, the check was liquidation, complex. It could also include transfer pricing issues. The taxpayer was an exporter of non-ferrous and ferrous scrap.

The study of the received cases established that some applicants pointed to the discrepancy between the acts of inspections and the requirements of the legislation, including the tax one.

Requirements on the need for a detailed description of violations of the tax legislation of the Republic of Kazakhstan do not apply to audits conducted on transfer pricing issues.

In the case on the application of "Zh" LLP, in respect of which a thematic audit was carried out on transfer pricing issues, the court of the city of Astana in its decision reasonably indicated that the requirements for the need for a detailed description of tax violations the laws of the Republic of Kazakhstan cannot be applied to audits conducted on transfer pricing issues. The audit report clearly sets out the grounds and reasons for exclusion from the expense differential, as well as adjustments to the differential with reference to transfer pricing legislation. In the same case, the applicant, in support of procedural violations during the execution of the act of inspection dated December 30, 2016 No. 526, indicated that the inspection was carried out in accordance with the order and additional instructions, according to which the head of Department N. was included in the list of inspectors, however, the said act verification they are not signed.

The court found that, according to the order of the Department dated September 29, 2015 No. Zh-342, N. was appointed to the position of head of the department for the administration of imports of third countries and the Customs Union of the Office of Indirect Taxes.

According to paragraph 7 of Article 140 of the PC, the specifics of the procedure, the terms for conducting, prolonging, suspending inspections, drawing up an act on the appointment, results and completion of inspections carried out by state revenue bodies are determined by the Tax Code.

Paragraph 6 of Article 637 of the Tax Code provides for the drawing up of an audit report in two copies, signed by the officials who conducted the audit, one copy of which is handed over to the taxpayer.

Meanwhile, on the date of completion of the tax audit, N. was working in another structural unit of the Department, his powers did not include the signing of this act of audit.

In this connection, the court concluded that the arguments of the applicant's representatives about a gross violation of the norms of the tax and entrepreneurial codes in drawing up the inspection report were not confirmed.

Since supporting documents were presented during the trial by representatives of the tax authority, the court correctly pointed out that there were no grounds for canceling the notice in these circumstances.

The fact of not issuing an additional order to replace (exclude) the persons conducting the inspection cannot be recognized as a gross violation, entailing the cancellation of the notification of the results of the inspection. This violation may be the basis for the courts to issue a private ruling.

On October 7, 2015, the decision of the supervisory authority of the Supreme Court annulled the judicial acts of the courts of the Mangistau region regarding the challenge by Corporation “C” of the notification of the Tax Department for the Mangistau region dated June 25, 2014 No. 269, case in this part, it was sent for a new consideration to the appellate judicial board for civil and administrative cases of the Mangystau Regional Court.

The supervisory court pointed out that, contrary to the requirements of the law, the 2008 transaction tax authority did not determine the specific amount of the deviation of the transaction price from the market price, and did not submit an annex to the audit report.

For transactions in 2009-2012, the tax authority did not indicate either the size of the price range values, or the size and components of the differential. The act made a reference to the application of calculations, but, as indicated above, they were absent in the case file (a more detailed description is given below).

Stability of the tax regime

Control over transfer pricing is not part of the tax regime, therefore its implementation is legal regardless of the provisions of subsoil use contracts on the stability of the tax regime.

Article 173 of the current Tax Code establishes that the tax authorities exercise control over transfer pricing for transactions in the manner and cases provided for by the legislation of the Republic of Kazakhstan on transfer pricing.

Similar provisions were contained in Article 654 of the 2008 Tax Code.

As an example, the case on the application of the Company “M” should be cited.

Company "M" operates at the Dunga field in the Mangistau region on the basis of a production sharing agreement concluded between the Government of the Republic of Kazakhstan and Companies "M", "O" and "P" on May 1, 1994 (as amended and supplemented on March 26, 2001 , May 24, 2002, December 28, 2015, March 1, 2016) hereinafter Dunga PDR.

The State Revenue Department for the Mangistau region conducted a thematic tax audit of the Company on the issue of transfer pricing for the period from January 1, 2009 to December 31, 2013.

Based on the results of the audit, an act of documentary tax audit No. 972 dated December 30, 2016 was drawn up and a notice was issued of additional CIT in the amount of 704,674,852 tenge and penalties in the amount of 181,685,976 tenge, the loss not subject to payment to the budget of 133,275,745 tenge has been reduced.

According to the Company's statement, tax liabilities in respect of the Dunga deposit are stabilized to the legislation of the Republic of Kazakhstan as of the moment of conclusion of the Dunga PSA and taxation should be carried out exclusively within the framework of the requirements of the Decree of the President of the Republic of Kazakhstan "On taxation of profits and income of enterprises" No. 1568 dated February 12, 1994 (hereinafter - Decree No. 1568).

Decree No. 1568 does not contain provisions obliging the Company to make adjustments to actually received income in accordance with transfer pricing legislation.

Transfer pricing legislation was introduced in the Republic of Kazakhstan only from January 5, 2001, has no retroactive effect and therefore cannot be applied to the Company's activities under the Dunga PSA.

The courts considered these arguments of the Company untenable for the following reasons.

The Law of the Republic of Kazakhstan on Transfer Pricing governs public relations arising from transfer pricing in order to prevent loss of government revenue in international business transactions and transactions related to international business transactions. The legislation of the Republic of Kazakhstan on transfer pricing is based on the Constitution of the Republic of Kazakhstan, consists of this Law and other regulatory legal acts.

In accordance with clause 10.5.1 of the Agreement on Amendments and Additions to the Dunga PSA dated December 28, 2015, concluded by the parties during the period of the audit, the Company agrees that tax administration is carried out in accordance with the tax legislation of the Republic of Kazakhstan in force at the time the obligations arise.

By virtue of Article 2 of the Tax Code of 2008, the tax legislation of the Republic of Kazakhstan is based on the Constitution of the Republic of Kazakhstan, consists of

this Code, as well as regulatory legal acts, the adoption of which is provided for by this Code.

Subparagraph 33) of paragraph 1 of Article 12 of the Tax Code of 2008 provides that the tax regime is the totality of the norms of the tax legislation of the Republic of Kazakhstan applied by the taxpayer when calculating all tax liabilities for the payment of taxes and other obligatory payments to the budget established by this Code (subparagraph 54) of paragraph 1 of Article 1 of the current Tax Code).

From the foregoing, it follows that transfer pricing legislation is not part of the tax legislation and control over transfer pricing is not part of the tax regime, relates to national security issues and its implementation is lawful, regardless of the provisions on the stability of the Dunga PSA tax regime.

The Company's arguments that tax stability was confirmed by the effective decision of the Astana City Court dated August 15, 2008, were not taken into account, since the subject of the appeal under the Dunga PSC was a notification of the accrued amount of taxes and other obligatory payments to the budget, not related to the control in the application of transfer prices.

Correlation between transfer pricing legislation and international agreements concluded by the Republic of Kazakhstan

In accordance with the Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations adopted by the Organization for Economic Co-operation and Development (OECD), the international standard transfer pricing method for OECD member countries is the arm's length principle.

This principle is also provided for by national legislation. Its definition is given in subparagraph 12) of Article 2 of the Transfer Pricing Law. The "arm's length" principle is the principle used to determine the market price, taking into account the range of prices, based on a comparison of the terms of transactions between related parties with the terms of transactions between independent parties carrying out transactions at a market price determined in the manner prescribed by this Law.

At the same time, unlike the practice of OECD member countries, the legislation of Kazakhstan provides not only subjective, but also objective criteria for determining the scope of control over transfer pricing.

Such a conclusion follows from the definition of the transfer price concept contained in subparagraph 25) of Article 2 of the Transfer Pricing Law. According to this rule, the transfer price (transfer pricing) is a price that is formed between related parties and (or) differs from the objectively formed market price, taking into account the

range of prices between independent parties, subject to control in accordance with this Law.

That is, state control over pricing can be exercised not only on transactions between related parties, but also on transactions between independent parties. The transfer price will be recognized as the price, which, although formed between independent parties, differs from the market price.

In the course of the generalization, it was found that such applicants as Company “M”, LLP “Zh”, when challenging notifications based on the results of inspections, pointed out the violation by the tax authorities of international conventions on the avoidance of double taxation, which provide for control over income only between related parties. Whereas they entered into transactions only with unrelated parties.

The courts did not take into account the applicants' arguments. Based on the provisions of subparagraph 25) of Article 2 of the Transfer Pricing Law, they came to the conclusion that not only transactions of related parties, but also transactions of independent parties are subject to transfer pricing control.

At the same time, the transfer pricing control of the party to the transaction, which is a resident of the Republic of Kazakhstan, does not violate international agreements on the avoidance of double taxation, to which the Republic of Kazakhstan is a party, since the other party to the transaction, the counterparty of the resident, is not subject to such control and is not taxed in the Republic of Kazakhstan.

Therefore, verification of the Company's activities within the framework of the requirements of the Law does not violate the norms of international agreements.

Limitation period

According to paragraph 10 of Article 46 of the 2008 Tax Code, in the event that requests are sent during a tax audit in accordance with the legislation of the Republic of Kazakhstan on transfer pricing, the limitation period in terms of reviewing the calculated, assessed amount of taxes and other obligatory payments to the budget is suspended for the period of sending requests and obtaining documents and (or) information on them. The total limitation period for the revision of the calculated, accrued amount of taxes and other obligatory payments to the budget, taking into account its suspension, cannot exceed seven years.

Similar provisions are contained in paragraph 10 of article 48 of the 2017 Tax Code.

Subparagraph 1) of paragraph 1 of Article 4 of the Law on Transfer Pricing provides that the authorized bodies, for the purposes of exercising control, have the right to

request from participants in transactions, state bodies and third parties information necessary to determine the market price and differential, as well as other data for monitoring transactions.

Sending a request for information necessary to determine the market price and the differential complies with the requirements of transfer pricing legislation and entails the suspension of the limitation period.

In support of its disagreement with the adjustment of income for 2010, LLP "Zh" indicated that the limitation period is 5 years and none of the grounds provided for the extension of the period is applicable to the activities of the Partnership.

The court found that the tax audit scheduled on December 29, 2014 was completed on December 30, 2016. During this period, the inspection was suspended and resumed, about which notices were issued, which were handed over to the Partnership.

According to letters dated December 31, 2014 No. SD-9.2-9-1320 and dated June 12, 2015 No. MKD-12-2/419, the Department requested information from Thomson Reuters about the provision of information on prices for Brent dated crude oil, Urals RCMB, Urals Med, Iranian Light for the period from January 1, 2009 to December 31, 2013.

Thus, the reason for the suspension of the audit was the sending of requests for information to Thomson Reuters.

The court pointed out that the suspension of the term for the tax audit did not contradict the requirements of paragraph 4 of Article 629 of the Tax Code. At the same time, according to paragraph 5 of this provision, the period of suspension on the grounds established by paragraph 4 of this article is not included in the term of the tax thematic audit of legal entities on transfer pricing issues.

Guided by subparagraph 1) of paragraph 1 of Article 4 of the Transfer Pricing Law, the tax authority exercised the right to send a request for information necessary to determine the market price and differential to Thomson Reuters, which is one of the world's largest international agencies that publishes, among other things, differential information.

In this regard, the court considered that the total limitation period for the tax liability and the claim for the tax audit in question was complied with and did not exceed seven years, in connection with which the arguments of the Partnership about the omission of the limitation period for 2010 were not taken into account by the court and rejected due to unreasonableness .

Sending a single request within the framework of simultaneous checks to control the application of transfer pricing in relation to several subsoil users, suspends the running of the limitation period for all inspections in relation to all inspected entities.

Company "M", challenging the accrual of taxes for 2009-2010 beyond the limitation period, pointed to a violation by the tax authority of the norm of paragraph 10 of Article 46 of the Tax Code. Evidence that requests were made during the course of the audit by the latter was not provided.

The tax audit scheduled by the State Revenue Department for Mangystau region on December 29, 2014 was completed on December 30, 2016. The reason for the suspension of the audit was the sending of a request to Thomson Reuters dated December 31, 2014. Meanwhile, the request was sent by the State Revenue Department for the city of Astana.

The court concluded that the statute of limitations had been met. It was decided to send a single request to Thomson Reuters in order to obtain information regarding the checks carried out simultaneously at that time to control the application of transfer pricing in relation to several subsoil users in the Republic. Price information was obtained from the Thomson Reuters electronic database, accessed by the Department after payment for services at the end of 2016 (i.e. at the date of completion of the audit).

These circumstances are confirmed by the contract for the provision of services by Thomson Reuters (UK) dated July 16, 2014 No. 1-8451218963 and invoices payable dated December 20-21, 2016.

Since the arguments of the tax authority were supported by written evidence, the courts indicated that the limitation period for the period 2009-2010 provided for by paragraph 10 of Article 46 of the Tax Code had not been missed.

The provisions of the Law on Transfer Pricing do not provide for the procedure for determining taxable income, but regulate the mechanism for adjusting prices applied in international business transactions. In this regard, when exercising state control over the use of transfer prices, the provisions of the subsoil use contract are not subject to application.

This conclusion was made by the specialized judicial board of the Supreme Court when considering the case on the application of the Company "M". According to the Company's statement, when calculating adjusted income, the Department took into account all proceeds from the sale of oil, without taking into account the provisions of the Dunga PSA, the Joint Venture Agreement dated August 9, 2001, the Operating

Agreement regarding marketing, transportation and sales of oil and gas from January 1, 2017. The Company's total income from oil sales is 87.2% of the total volume of oil sold, of which: 52.32% belongs to the Company, 17.44% - to company "P" and 17.44% - to company "O". 12.8% of the total volume of oil sold belongs to the Kazakh side. Accordingly, the Company's taxable income includes only the income received from the sale of its share of oil. The sale of the oil share of the Kazakh side is carried out on the basis of letters of instruction from JSC "K" and the Ministry of Oil and Gas of the Republic of Kazakhstan and the ownership of this share is not transferred, all the proceeds from the sale of the shares are transferred to the income of the Republic of Kazakhstan.

Satisfying the Company's application in this part, the court of first instance proceeded from the fact that the applicant did not acquire the ownership of the shares of the Kazakh side and partners, he was not obliged to pay taxes on the proceeds from the sale of these shares. Accordingly, the amounts received from the sale of these shares should not be included in the Company's taxable income.

The court of appeal recognized these conclusions as contradicting the requirements of the legislation and not corresponding to the circumstances of the case.

By virtue of Article 392 of the Civil Code, when interpreting the terms of the contract, the court takes into account the literal meaning of the words and expressions contained in it. The literal meaning of the terms of the contract in case of its ambiguity is established by comparison with other terms and the meaning of the contract as a whole.

In accordance with section 9.1 of the Dunga PSC as amended in the 2015 Agreement, the payment of the share due to the Kazakh side is made by the Contractor (Company) in cash to the appropriate budget classification code.

By virtue of clause 10.5.2 of the Dunga PSA, as amended in the 2015 Agreement, the Contractor agrees that section 10.5.1 (in terms of providing tax forms, conducting tax audits, paying taxes, fines and penalties) also applies to the share of the Kazakh side, calculated in accordance with with Article IX of the DRP. Such share of the Kazakh side is not a tax, but represents only a contractual obligation.

In accordance with the provisions of Article IX of the PSA Dunga Contractor has the exclusive right to receive at its disposal in each quarter such amount of oil and gas net production for each calendar year. The Kazakh side is entitled to receive its share as a percentage of the remaining net production.

Under paragraph 1.24, "Net Production" means the amount of oil and gas produced in the sub-contract area under the PSA.

By virtue of Article XI of the PSA, Dunga Contractor maintains financial records relating to oil and gas operations under the PSA.

Thus, when oil is sold, the entire proceeds are attributed to the Company's income. And only subsequently does the Contractor have a contractual obligation to pay the share to the Kazakh side in percentage terms.

Section 12.4 of the Dunga PSC, as amended on May 24, 2002, provides that partners have the right to establish their own internal procedure for the distribution of income and expenses, regardless of the share of participation. That is, all costs incurred in connection with activities will be distributed in accordance with internal agreements.

In accordance with paragraph 6 of Article 10 of the Law, based on the adjustment of objects of taxation and (or) objects related to taxation, taxes and other obligatory payments to the budget are paid, calculated in such a way as if the income or expenses from these transactions and other objects of taxation for the reporting period were determined based on the market price, taking into account the range of prices, with the application of fines and penalties in accordance with the legislation of the Republic of Kazakhstan.

The norms of the Law do not provide for the procedure for determining taxable income, but regulate the mechanism for adjusting prices applied in international business transactions. In this regard, when exercising state control when applying transfer prices, the provisions of the contract for subsoil use are not subject to application.

A Contractor is a participant in international oil export transactions and submits reports on the export of goods (works and services) to the authorized body.

In such circumstances, the Department correctly treated the entire amount from the sale of oil as the Company's total annual income and taxable income.

In this regard, the court of appeal annulled the decision of the court of first instance in this part with a new decision to refuse to satisfy the Company's application.

When establishing the fact of a deviation of the transaction price from the market price by more than 10 percent, the tax authority must determine the specific amount of the deviation.

In accordance with paragraph 1 of Article 3 of the Law on State Control over the Application of Transfer Prices, state control over the application of transfer prices in international business transactions (hereinafter referred to as the State Control) is carried out in order to establish the fact of deviation of applied prices from market prices for transactions specified in paragraph 2 of this article, and adjustment of taxable items. Paragraph 2 establishes that for international business transactions that are not subject to subparagraphs 1) - 6) of this paragraph, state control is carried out if it is established that the transaction price deviates by more than 10 percent in one direction or another from the market price of goods (work, services).

The current Law on Transfer Pricing requires establishing the fact that the transaction price deviates from the market price by more than 10 percent only for transactions with agricultural products.

The requirement specified in the law indicates that, based on the results of the audit, the tax authority should establish a specific amount of deviation exceeding 10 percent.

Consideration of the cases showed that the tax authorities do not always comply with these requirements.

Thus, the Department of State Revenues for the Mangistau region conducted a documentary thematic audit of the branch of Corporation "C" on transfer pricing for 2008-2012.

Since in 2008 the Corporation sold oil to an unrelated party, the tax authority applied the above provision of the 2001 Law. On pages 3 and 4-5 of the inspection report, it is indicated that there is a deviation in the transaction price by more than 10% from the market price and the amount of adjusted income in the amount of 40,196,374 tenge. It is also indicated that the table for calculating the deviation of the prices of the branch's transactions from the market prices is attached (Appendix 2008-2).

The corporation in a statement pointed out the absence of a description of the violation of the law in the inspection act in relation to 2008.

As the examination of the case by the supervisory instance of the Supreme Court showed, the applicant's arguments were not properly examined by the courts of the Mangystau Region.

Attached to the case file, the act of verification, consisting of 11 pages, did not contain any appendix. Moreover, the appendix with the calculations was completely absent from the case file.

Having indicated in the act of checking for the presence in 2008 of a deviation in the transaction price by more than 10% of the market price, the tax authority did not determine the specific amount of the deviation. At the meeting of the court of the supervisory instance, the tax authority could not give an answer on this issue, explaining that in local courts this issue was not raised or investigated before it. It was not submitted to the court of the supervisory instance and the annex to the act of verification.

These circumstances, together with other violations, led to the cancellation of judicial acts and the referral of the case for a new trial to the court of appeal.

Based on the results of the re-examination of the case, the court of appeal found the applicant's arguments substantiated.

The conducted generalization showed that the subject of the court proceedings were the issues of transfer pricing for export transactions.

For the purpose of determining the market price, the comparable uncontrolled price method was mainly used. Sometimes cost-plus methods and resale prices were used.

According to paragraph 1 of Article 13 of the Transfer Pricing Law, the comparable uncontrolled price method is applied by comparing the transaction price for goods (works, services) with the market price, taking into account the range of prices for identical (and in their absence, homogeneous) goods (works, services) in comparable economic conditions.

The named traditional method is used within the framework of the "arm's length" principle. It compares the price charged for property or services transferred in a controlled transaction with the price charged for property or services transferred in a comparable uncontrolled transaction under comparable conditions.

Paragraph 4 of Article 13 of the Transfer Pricing Law establishes that when applying the comparable uncontrolled price method, the market price is determined as follows:

1) for transactions with goods (works, services) for which there is documented information on the route of transportation to the relevant market, where there is a price in the information source, the market price is determined as the price from the information source, taking into account the price range. The transaction price is given by means of a differential to comparable economic conditions with the market price;

2) for transactions with goods (works, services) that do not comply with subparagraph 1) of this paragraph, the market price is determined by bringing the price from the

information source in the relevant market by means of a differential to comparable economic conditions with the transaction price, taking into account the price range.

Paragraph 5 of the same article indicates the components of the differential, which, by virtue of the requirements of paragraph 6, must be confirmed by documents or sources of information.

The study of cases and judicial acts found that most of the controversial issues arise in connection with the application of the provisions of Article 13 of the Transfer Pricing Law, including the determination of the components of the differential.

Transfer pricing for oil transactions

Paragraph 2 of Article 13 of the Transfer Pricing Law determines that if the quotation period established in the contract for the sale of goods (works, services) does not correspond to the conditions for determining the quotation period established by this article, market prices for goods (works, services) are accepted at the time of sale this product (work, service).

This norm was reasonably applied by the tax authority based on the results of the audit of K LLP.

The facts of the use of transfer prices by the taxpayer have been established in transactions made with companies "T" (Netherlands), "TH" and "V" (Switzerland) on the terms of FOB delivery of the CPC terminal (sea terminal of CPC-R port of Novorossiysk, Yuzhnaya Ozereevka) to the Mediterranean countries . According to the calculations for 2012, the amount of adjusted income amounted to 403,519,311 tenge.

In the sale and purchase agreements, the price of oil per 1 barrel was determined according to the formula, which provides for Spread CPC FOB 80KT (the average value of average Spread CPC FOB 80 KT) in the calculations for the period from 15 to 21 calendar days before the first day of loading, approved by the CPC-R schedule . However, the use of the said amount of Spread CPC FOB 80 KT did not meet the conditions for determining the quotation period established by the Transfer Pricing Law.

Disputing the position of the tax authority, the applicant pointed out that the prices of oil under transactions do not deviate from market prices, since for the components of the differential, in particular, the difference in oil quality - Spread CPC FOB 80 KT, the quotation period is not provided for by the Transfer Pricing Law.

By virtue of subparagraph 3) of Article 2 of the Transfer Pricing Law, the quotation period is the pricing period established in the contract for the sale of goods, during which the parties to the transaction determine the value of price quotations for exchange goods.

Since pricing is the formation of prices from certain components, in this case according to the formula: Price = Brent + Spread CPC FOB 80KT - X, then to determine the price for a certain time, it is necessary to take the value of these components for the same quotation period.

According to subparagraph 1) of paragraph 2 of Article 13 of the Transfer Pricing Law, for the purposes of this Law, the quotation period must be determined in accordance with the terms of the contract in the temporary interval: for oil when selling goods by sea, no more than five quotation days before the date of transfer of ownership of the goods to the buyer and no more than five quotation days after the date of transfer of ownership of the buyer to the goods.

In this case, the taxpayer sold oil by sea and the price for 1 barrel of oil was determined by applying in the above formula the average quotation of Brent (Dated) for 5 calendar days after the date of the bill of lading and the average quotation of Spread CPC FOB 80 KT for the period from 15 to 21 calendar day prior to the first day of loading approved by the CPC-R schedule (that is, as stipulated by the contract - an oil purchase and sale transaction).

Since the quotation period established in the contract for the sale of oil does not meet the conditions for determining the quotation period established by subparagraph 1) of paragraph 2 of Article 13 of the Transfer Pricing Law, the tax authority correctly accepted market prices for oil at the time of the sale of this product (as of the date of the sea bill of lading). Accordingly, deviations of transaction prices from market prices were correctly identified and income was adjusted, which resulted in additional CIT and penalty charges.

Incorrect application of quotations was established during the audit of JSC K, which exported crude oil on FOB delivery terms: Novorossiysk, Yuzhnaya Ozereevka, Odessa, Primorsk, DDU No. 704 Odessa.

Both the taxpayer and the tax authority, in order to determine the market price, used the comparable uncontrolled price method, as well as the official source of information "Platt's Crude Oil Marketwire" (published by "The Mc Graw-Hill Companies", UK), approved by the Decree of the Government of the Republic of Kazakhstan "On Approval of the List of Official Sources of Information on Market Prices for Certain Types of Goods Subject to State Control when Applying Transfer

Prices in International Business Transactions” dated June 9, 2001 No. 788. as well as other sources of information.

In 2009, the buyer of a part of the export volumes was the company TH, registered in Switzerland.

In accordance with the Decree of the Government of the Republic of Kazakhstan dated December 31, 2008 No. 1318, Switzerland is included in the list of states with preferential taxation and, in accordance with paragraph 12 of Article 10 of the Transfer Pricing Law, the differential does not affect transactions, the participants of which are registered in a state with preferential taxation, and the adjustment of objects taxation and objects, related to taxation is made without taking into account the provisions of paragraph 5 of Article 13 of the Transfer Pricing Law.

The taxpayer sold crude oil to company “T” on delivery terms FOB Yuzhnaya Ozereevka - CPC FOB 80kt quotations were used, FOB Novorossiysk - URALS (EX-NOVO) FOB 80kt quotations, which are indicative (calculated), that is, not formed through supply and demand.

The tax authority, when calculating the deviations of the prices of the taxpayer's transactions from the market prices for transactions from the sale of oil on the terms of delivery of FOB Yuzhnaya Ozereevka, FOB Novorossiysk, used the CPC Blend CIF and URALS (RCMB) quotations formed on CIF Augusta using transportation and associated costs by converting them into comparable economic conditions with the taxpayer's transactions, that is, with reduction to the delivery basis FOB Yuzhnaya Ozereevka, FOB Novorossiysk.

Under such circumstances, the conclusions of the tax audit on the application of the CPC Blend CIF and URALS (RCMB) CIF quotations, formed on the CIF of August, when calculating the deviations of the prices of the taxpayer's transactions from market prices for transactions from the sale of oil on delivery terms FOB Yuzhnaya Ozereevka, FOB Novorossiysk, were recognized by the court legitimate.

1. Subparagraph 1) of paragraph 5 of Article 13 of the Transfer Pricing Law determines that the differential includes expenses that are justified and confirmed by documents and (or) sources of information necessary for the delivery of goods (works, services) to the relevant market.

This type of differential components is the most diverse and depends on the terms of delivery of the goods.

The following issues were considered by the courts:**1.1. Cargo insurance**

The court found it unreasonable to use the source of information in the presence of documents confirming the buyer's expenses for cargo insurance.

The tax authorities, without contesting the inclusion of cargo insurance costs in the differential, applied the amount of the differential from the official source of information.

Taxpayers took the indicator based on documents submitted by insurance companies.

According to the statements of LLP "K", Company "M", LLP "Ka", the court found it unreasonable to use the source of information if there are documents confirming the buyer's expenses for cargo insurance, such as debit notes, invoices issued by the insurance company for each shipment.

In the presence of documents confirming the buyer's expenses for cargo insurance, the Department unreasonably applied information from information sources.

Regarding the insurance costs of JSC "K", the court agreed with the conclusions of the inspectors about the need to use information from the source "Argus Media", since the taxpayer presented copies of letters from the insurance company as evidence, while these costs must be confirmed by the relevant service contracts, invoices - invoices (invoices).

Zh LLP, as evidence confirming insurance expenses, submitted documents from company C, registered in a state with preferential taxation (People's Republic of China in part of the territory of the Hong Kong Special Administrative Region), in accordance with paragraph 12 of Article 10 of the Transfer Pricing Law data costs cannot be taken into account when determining the market price.

Letters from buyers also cannot serve as documentary evidence of the costs included in the differential, since compulsory insurance is carried out during sea transportation.

1.2. Costs for agency, aerobatics and ship calls,accounted for by JSC "K" are excluded from the differential in accordance with subparagraph 1) of paragraph 5 of Article 13 of the Transfer Pricing Law due to the lack of documentary evidence.

1.3. Costs for the transportation of goods from the point of delivery Adamowa Zastawa to the port of Gdansk

The legislation governing transfer pricing provides for the determination of the market price, taking into account the costs of the buyer for the transportation of goods after the transfer of ownership.

These expenses are completely excluded from the composition of the differential based on the results of the audit of K LLP.

The court agreed with the arguments of the tax authority in this part. Thus, the cost of transporting goods from the Adamowa Zastava oil delivery point to the port of Gdansk, carried out under the contract dated December 23, 2009, provides for the terms of FOB delivery to the port of Gdansk.

The INCOTERMS-2000 rules mainly determine the obligations, costs and risks arising from the delivery of goods from the seller to the buyer.

FOB - free on board, means that the seller delivers the goods on board the vessel nominated by the buyer at the named port of shipment. The risk of loss or damage to the goods passes when the goods are on board the ship and from that moment the buyer bears all costs.

Thus, the FOB delivery terms confirm the conclusions of the audit that the costs of transportation from the Adamowa Zastawa oil delivery point to the port of Gdansk are the seller's expenses and should not be reflected in determining the market price.

The applicant's arguments that the buyer bears these transportation costs under the terms of the contract were declared untenable by the court. In supplementary agreement No. 2 to the contract KTM / VCA-2010 dated December 23, 2009, the buyer undertook to additionally assist the seller in transporting the oil that remained in the seller's ownership along the route PSN Adamowa Zastava - the port of Gdansk. Transportation costs, losses and other costs associated with transportation will be reflected in the price differential.

The parties to the transaction are free to choose the terms of delivery of the goods and the costs of its delivery, however, the legislation governing transfer pricing provides for the determination of the market price, taking into account the costs of the buyer for transporting the goods after the transfer of ownership. If the buyer bears the costs of transportation to the port of loading, the buyer has the right to issue an invoice to the seller for payment of these costs. Therefore, the inspectors rightfully excluded the costs of transporting oil from the Adamowa Zastava oil delivery point to the port of Gdansk when determining the objects of taxation in 2010.

Similarly, expenses for the transportation of goods from the Adamova Zastava oil delivery point to the port of Gdansk and from K LLP were excluded.**1.4. Discount for the supply of a non-tanker oil consignment**

When determining the market price in 2009-2010, LLP "K" applied the differential for the supply of a non-tanker oil lot only according to the buyer's transcript, no other

evidence was provided confirming the buyer's expenses for incomplete filling of the tanker with goods.