

Enquiry stage: how to prevent it from becoming tax control or audit 2/46/24



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For over a year we have been living with the new system the State Revenue Service (SRS) uses for checking individuals and entities. Amendments to the Taxes and Duties Act outline a different approach to tax administration aimed at simplifying and improving current checks in favour of the individual. This approach provides for only three stages: enquiry (obtaining information), tax control, and audit. These are not always consecutive steps and there may be different combinations. For example, enquiry can go straight into audit, tax control can move into audit, and enquiry may well end your communication with the SRS. Our experience suggests that carefully preparing your response to an SRS information request can reduce their interest in you and prevent the enquiry stage from changing into a more serious tax review.

What should you know about the enquiry stage?

Enquiry is an independent process that can be run outside any particular review. However, your obligation to respond and cooperate remains.

The SRS basically uses the information received in three ways:

1. To evaluate any doubts and discrepancies
2. To prevent breaches by asking the taxpayer to voluntarily eliminate any breaches and discrepancies found
3. To decide whether there are grounds for launching an administrative procedure (i.e. for starting some type of tax review) or an administrative offence procedure (to hold the taxpayer liable for committing an administrative offence)

Enquiry involves not only requesting documents or explanations but also:

- Assessing and analysing the information on the taxpayer available to the SRS
- Checking the information and documents filed by the taxpayer
- Visiting (inspecting) the taxpayer's business areas and premises
- Monitoring the taxpayer's economic activity
- Making control purchases
- Virtual visits

Recommendations

Cooperate actively and answer SRS questions accurately and comprehensively

You have every opportunity to stop any further interest in you at this stage, so take it! This advice might seem obvious but our experience suggests that taxpayers' explanations are often very general, inconsistent and inaccurate. Of course, this behaviour mostly stems from not knowing what to do or from failing to realise that your answer should be far more elaborate. It's advisable to support your explanations

with documentary evidence at this stage already.

For example, many people are currently preparing explanations in response to an SRS information request about discrepancy between amounts received in their bank accounts and their total reported income. In several cases the reason for such discrepancy is transfers between your own accounts when the same amount is recorded twice (first in the account it enters and then in the one it's transferred to). So your explanations might come with printouts from your accounts giving information on your incoming payments.

Another reason the SRS information does not match your account turnover might be child support, for instance. Under section 9(1)(11) of the Personal Income Tax (PIT) Act, child support (maintenance) is excluded from annual taxable income and is not taxed, so child support does not create additional taxable income. To confirm that incoming amounts are indeed child support, you can present your parental agreement on child support, a court order for child support, and other evidence. If the total child support received exceeds EUR 10,000 for the year, the taxpayer is liable to report this income (there is still no taxable income). So if you find such an excess, you will be liable to adjust your annual income tax return. If the amount received is less, then your explanations should state that you received child support and you were not liable to report this income separately under section 19(2) of the PIT Act. Here we need to add that you should check whether your other non-taxable income together with child support exceeds EUR 10,000 for the year, because in that case you would have to report all non-taxable items of income received during the year on your annual income tax return (even if each item alone did not exceed EUR 10,000).

Clarify unclear questions

If you are not clear about something, answer as best you can, but leave yourself a chance to modify your answer or to ask whether you have understood a particular part of the information request correctly, and to ask the tax authority to confirm your understanding or to clarify the question. The SRS will often frame their questions such that even subject-matter experts are unable to figure out what is needed. And we have noticed that the SRS tend to use information request templates (i.e. a comprehensive information request created once is then tailored to a new request for another taxpayer). Such template questions will not always fit your particular situation or the nature of your economic activity, so it's worth checking what they meant by one or other question.

Evaluate the need for the information provided

The SRS often exaggerate the amount of information being requested, for example, they might want to see all your invoices or all your supporting documents and supplier contracts for the last two years. A company can have hundreds of transactions for the relevant period. If you explain this properly, the SRS might agree to reduce the amount of required documentation and might ask you to send documents only for particular (selected) transactions or for larger transactions within the period under review.

However, the amount of information being requested may become uncontrollable at some point. Our experience suggests the SRS can request additional information repeatedly, with each subsequent request becoming even larger. This raises the question whether we are still at the enquiry stage or whether it's already an in-depth review covertly going on, with no clear limits, statutory deadlines or other restrictions. This is where our next piece of advice comes in.

Ask for a meeting/call with tax inspectors

Setting up a meeting or conference call with tax inspectors will not only help you better understand why the information is being requested but will also give you a chance to discuss any unclear questions, agree on a more reasonable approach to the amount of information being requested, or in certain cases dispel the tax authority's doubts about your particular situation, business model and elements of economic activity.

If you follow these relatively simple pieces of advice, chances are the SRS will have no grounds for launching a tax control or audit.