

Grigol Chkhaidze*

Changing the Classification of a Business Transaction based on Its Form and Substance in Tax Law Relations

Tax law relations are known by their complexity. Generally, tax law-related relations always derive from civil relations, where people participate. Income tax is due when a person is employed, or is self-employed and conducts economic activities. Value Added Tax is due when a taxpayer conducts economic activities and such economic activities are based on different types of contracts. The taxpayer supplies goods or services to the end-users and therefore, is obliged to pay Value Added Tax.

There are many cases when parties conduct a contractual agreement, which does not reflect economic reality. Article 73 (9) of the Georgian Tax Code gives Georgian Tax Authorities the possibility to change the form when the substance does not collide with the form. But the legislation is very general and does not include any indication or legal prerequisites on how this should be done.

This article will serve a purpose to define in which cases tax authorities are allowed to change the form of the business operation, especially when the parties conducted completely different contracts and will evaluate the risks, which might be in presence if the tax authorities will use the norm in a wrong way.

This article will review tax authority's practices and the Georgian Court approach towards the issue.

Key Words: *Tax, Tax System, Directive, Tax Code, CJEU, Substance and form, Georgian Court System.*

1. Introduction

For taxation purposes, it does not matter if the transaction is legal or not.¹ Even though certain business activities might require a special permit and a taxpayer conducts such activity without holding a valid license, for the purpose of the Tax Code, this activity is still taxable, and therefore, taxes will be levied.

Generally, tax law-related relations always derive from civil relations, where people participate. Consequently, the form of contract and the relationship between the parties must be evaluated by the legislation which regulates the very contractual agreement the tax authority studies.

To achieve the main goal that every relationship will be evaluated correctly based on the form and substance, the legislation must be precise, stating all the necessary preconditions.² Tax legislation

* Doctor of Law, LLM, Lund University, Visiting Lecturer at Ivane Javakhishvili Tbilisi State University, Faculty of Law.

¹ Rogava Z., Tax Code Commentaries, Tbilisi, 2012, 479 (in Georgian).

² Gordon R. K., Thuronyi V., Tax Legislative Process in Tax Law Design and Drafting, Thuronyi V. (ed.), Washington D.C., 1996, 2.

in the process of drafting receives less attention in developing countries, comparing to other, developed countries. For example in the United States of America, any tax legislation and any changes relating to taxes involve big groups which are completed by the people of different professions.³ The main objective of such groups is that they will evaluate legislation from a different perspective which will guarantee that the law will be effective in practice.⁴

Any operation should be evaluated by its form and substance and it is vital, as it gives the taxpayer a legitimate expectation of how this operation will be taxed based on the legislation requirements. If the tax authorities have a broad possibility to evaluate the operation, which is the case nowadays based on the Georgian Tax Code, it does not give taxpayers the sense of stability and therefore, does not create a safe environment for them to operate in a predictable way. The more precise the legislation is which will grant tax authorities the possibility to change the form and substance of an operation, the more stable tax practice will be for the tax authorities and the Georgian Courts as well. Therefore, the purpose of the paper is to determine the preconditions for the change of the form of a business operation by the authorized administrative body, especially when an existing agreement between the parties carries out a completely different legal essence. Accordingly, the article presents the practical significance of the ability of a tax authority to change the form and content of a business operation as well as its legal grounds, which in turn requires an economic understanding. Additionally, the paper reviews the problematic issues that can be arisen when there is no distinct legal precondition defined by the law.

2. Comparison of the Contractual Relationship and Economic Factors while Examining Taxable Transaction

As *Prof. Zimmer* mentions for evaluating tax law-related relationships, it is necessary to take into consideration all the facts and right interpretation of the law, which regulates this very relationship.⁵ To evaluate tax-related relationship correctly, it is of vital importance that the judge or administrative body points out the following facts:

- The Reality of legal relationship;
- Economic reality;⁶

Therefore, while discussing the topic, in the first place should be checked whether the legal relationship is real or not. The judge or administrative body should clarify what type of obligations and rights arise from the legal relationship for parties from the contract. While examining the nature of the legal relationship, it also should be taken into account what type of obligations lies for each party in the contract and what are their rights.

Additionally, the second component, which means checking economic reality takes into consideration all the factors, which is related to the first component – the legal relationship between parties. (For example in a financial lease there might be a clause in the contract which indicates that at

³ Ibid.

⁴ Ibid.

⁵ *Zimmer F.*, Form and Substance in Tax Law – General Report, The Hague, 2002, 16-97.

⁶ Ibid, 28.

the termination of the contract the lease becomes the owner of the property, which indicates for economical purposes that the lease fee is part of the property value).⁷

Generally, while checking those two components – the legal relationship between parties and economic reality complies with each other. Sometimes, there is a divergence between those two and there is some vagueness which component should be taken into consideration while evaluating the tax consequences.⁸ In such cases, there are some opinions that tax authorities should completely ignore the essence of the contract which was the original agreement between parties, and taxes should be levied based only on economic reality.⁹ By following those opinions, it may be concluded that the contractual agreement and legal relationship between parties can be completely disregarded and the only factor which should be taken into consideration is economic reality.

Even though the above-mentioned approach seems reasonable, it has been criticized many times. A different approach suggests that considering only economic factors while evaluating the business operation is against core principles of the law and using it blindly should be strictly prohibited.¹⁰

For example, some national legislation defines what can be considered as an employment contract and this activity due to other national legislation might not be considered as a labor relationship. Consequently, “income” which is defined by national legislation defines a specific income type, which after being classified as such, might be taxed according to income tax rules. But if a person operates between two countries, in which one defines his/her income as an income derived from labor relations and the other country does not, s/he might be taxed twice which will be against the core principle of double taxation. Therefore, even from the economic point of view for both countries person received an income, it is crucial to analyze legal terms and contract nature for the best possible approach.

As *Prof. De Broe Luc* mentions, analyzing certain transactions only from an economic point of view is abstract and cannot be relied on, as there is always a legal relationship between parties which indicates what was an original agreement between parties and what was their aim while signing the contract.¹¹

Additionally, it is very important how the law will be interpreted. To have lawyers and economists on the same page while evaluating and interpreting the law, it is very important that in process of drafting the legislation both professions will be actively included. The law and its

⁷ *Li J.*, Economic Substance: Drawing the Line between Legitimate Tax Minimization and Abusive Tax Avoidance, *Canadian Tax Journal*, Vol. 54, Issue № 1, 2006, 43-44.

⁸ *Rosenblatt P.*, General Anti-Avoidance Rules for Major Developing Countries, *Series on International Taxation*, Vol. 49, Kluwer Law International, 2015, 138.

⁹ *De Broe L.*, *International Tax Planning and Prevention of Abuse: a Study under Domestic Tax Law, Tax Treaties and EC Law in Relation to Conduit and Base Companies*, IBFD Publications, Amsterdam, 2008, 168.

¹⁰ *Rosenblatt P., Tron Manuel E.*, Anti-Avoidance Measures of General Nature and Scope – GAAR and Other Rules, *IFA Cahiers*, Vol. 103A, International Fiscal Association, Rotterdam, 2018, 14.

¹¹ *De Broe L.*, *International Tax Planning and Prevention of Abuse: a Study under Domestic Tax Law, Tax Treaties and EC Law in Relation to Conduit and Base Companies*, IBFD Publications, Amsterdam, 2008, 170.

interpretation are different for lawyers and economists. Consequently, in process of drafting the law, it should be written in a way that will exclude possibilities for it to be read differently.¹²

As the international fiscal association reports in the 2018 edition, evaluating relationships from an economic point of view is not consistent and therefore it gives everyone the possibility to define it differently than it was supposed to be interpreted.¹³ In any case, if the form and substance of the contract are changed by the tax authorities, it will be different via countries, because every country has different mechanisms to fight against tax evasion and fraud. The only solution to overcome this challenge is the very tight cooperation of the national courts and tax authorities, as their practice leads a country to have one, uniform tax system.¹⁴

It is clear, that evaluating business transactions based only on the legal relationship between parties, will not give a clear image, as there are some cases, even when parties agree on certain terms and therefore they define the form of the contract, but it does not reflect the real substance of the contract.

3. Types of Contracts

There are scholarly opinions that changing the form of the contract based on the fact that substance is superior before form when there is a legal relationship between parties is strictly prohibited.¹⁵

Any relationship is regulated by the specific legislation, therefore tax legislation does not respond to the fact of what the parties intended to be their agreement.¹⁶ The form of the contract is something that reflects legislative requirements and the substance is reflecting what the parties intended to agree upon. Tax authorities can change the qualification of the contract when there is a certain legal prerequisite and it is only allowed when the qualification should be reflecting the existing legislation.

The fact that the nature of the taxes is seen differently by lawyers and economists should also be taken into consideration.¹⁷ For example, for lawyers, Value Added Tax can be described as the tax, which is related to every fact where there is a transaction. An additional term for Value Added Tax to be applicable for lawyers is that the transaction should be conducted by the registered person. It is very clear, that for lawyers for Value Added Tax to be applicable is that that two-term is in the picture.¹⁸ For economists, the main decisive factor is that there is a transaction, supply of goods, or service. As long as

¹² *Gordon R. K., Thuronyi V., Tax Legislative Process in Tax Law Design and Drafting, Thuronyi V. (ed.), Washington D.C., 1996, 2.*

¹³ *Rosenblatt P., General Anti-Avoidance Rules for Major Developing Countries, Series on International Taxation, Vol. 49, Kluwer Law International, 2015, 134.*

¹⁴ *Ibid, 12-13. See also: Li J., Economic Substance: Drawing the Line between Legitimate Tax Minimization and Abusive Tax Avoidance, Canadian Tax Journal, Vol. 54, Issue № 1, 2006, 53.*

¹⁵ *Rogava Z. Tax Code Commentaries, Tbilisi, 2012, 479 (in Georgian); See also: Uridia G., Tax Code Commentaries, Tbilisi, 2011, § 73.9, 486-491 (in Georgian).*

¹⁶ *Ibid, 487.*

¹⁷ *Sijbren C., A VAT Primer for Lawyers, Economists, and Accountants, The Vat Reader, Tax Analysts, 2011, 2, <[www.taxhistory.org/www/freefiles.nsf/Files/VATReader.pdf/\\$file/VATReader.pdf](http://www.taxhistory.org/www/freefiles.nsf/Files/VATReader.pdf/$file/VATReader.pdf)> [06.09.2022].*

¹⁸ *Ibid.*

there is a transaction, economists consider that the Value Added Tax is applicable.¹⁹ Therefore it is very clear that for economists it is less important to have all the formal requirements in place, while for lawyers it is crucial for deciding whether or not the transaction is taxable.²⁰ It should also be noted that for example if a person, unregistered is conducting business might still be reliable paying Value Added Tax, if there is a tax inspection and the tax authorities issue a fine, while from the economic point of view, this does not change anything regarding for the taxation purposes. For lawyers, it is the decisive factor and it is the main factor that influences the final decision on the issue.²¹

Taking into consideration all the above-mentioned examples, the conclusion can be derived that any operation from a different perspective can be evaluated differently, and therefore, while tax authorities might use the right to change the substance of the contract and rule it over the form, all the factors have to be taken into consideration.

For example, there is a service contract and the length of the contract is one year, and a person, receiving service pays a fee at the beginning of the month. This contract also has a clause that gives the recipient of the service possibility to cancel the contract, but the clause indicates that if the customer exercises this right, s/he will be fined and the fine will be equal to the amount what s/he had to pay for the whole year for the service. If the customer cancels the contract and pays the fine, from the economic point of view, the operation might be evaluated that the customer still paid the whole amount and the business operator received the equal amount of the money, therefore the amount of fee should be taxed. From the legal point of view, at the moment of the cancelation of the contract, the whole picture of legal relationship changes, and the agreement is no longer binding for the parties, the business operator does not supply service and consequently, the amount paid by the customer is qualified as a fine or compensation amount and not the fee paid for the service, which might indicate that the amount should not be taxed. This clearly shows that the one fixed term in the contract can be seen differently, which indicated the importance of the evaluation of any transaction from different perspectives

Additionally, any term for tax-related transactions might have a different meaning than it is indicated in the other legislation. For example, the term “consumption” which is the main core foundation to define whether the transaction is taxable or not in any other legislation means any type of consumption, while for the Value Added Tax purposes it only means final consumption from the end-user and only in such cases Value Added Tax is applicable.

4. The Practice of Georgian Courts

The conclusion from the above-mentioned examples can be derived that in any business operation, taking into account its complexity and individuality, any term or any substance can be

¹⁹ *Sjibren C.*, A VAT Primer for Lawyers, Economists, and Accountants, The Vat Reader, Tax Analysts, 2011, 2, <[www.taxhistory.org/www/freefiles.nsf/Files/VATReader.pdf/\\$file/VATReader.pdf](http://www.taxhistory.org/www/freefiles.nsf/Files/VATReader.pdf/$file/VATReader.pdf)> [06.09.2022].

²⁰ *Papis-Almansa M.*, Insurance in European VAT on the Current and Preferred Treatment in the Light of the New Zealand and Australian GTS System, Netherlands, 2016, 133.

²¹ *Henkow O.*, Financial Activities in European VAT, A Theoretical and Legal Research of the European VAT System and the Actual and Preferred Treatment of Financial Activities, Netherlands, 2007, 75.

recognized differently.²² To evaluate business transactions correctly, every factor must be examined which were used in the operation which is disputed. To evaluate all the factors is derived from the General Administrative Code of Georgia. The administrative body is obliged to fully examine all the necessary facts that are important to get the decision.²³ The same approach is repeated by the court practice created by the Supreme Court of Georgia. The decision states that the administrative justice is the core principle and it is one of the most procedural obligations for administrative body to examine and search every single fact related to the case and get the decision only based on those factors.²⁴ The imperative requirement declared by the General Administrative Code of Georgia serves public governance and legality principles, as any decision product of public governance should be derived from the very well-researched and evaluated facts.²⁵

The individual administrative act should be substantiated and it serves a goal to create some frame for administrative bodies and the frames will be directed only by the legislation. Any decision should be based on certain facts which will lead administrative bodies to get the final decision.²⁶ It is the facts and circumstances which will lead to the legal outcome of the case.²⁷

Furthermore, tax authorities, as a litigant in the court hearings, must prove that the administrative act issued by them is legitimate according to the Administrative Procedural Code article 17 (2). The burden of proof indicates the procedural obligation that the administrative body has to prove that they have studied all the necessary facts and all the necessary prerequisites have been fulfilled. The very obligation derives from the fact that the administrative act, if not appealed means that it is legitimate and the decision that they made is based only on legislation.

Article 64 of the Georgian Tax Code indicates that the tax assessment is the administrative act issued by the tax authority and it is legally binding.²⁸ As the tax assessment is the administrative act, all the obligations imposed by Georgian legislation to issue administrative act is applied to tax assessments too. Therefore, in case changing the taxable transaction form requires having all the facts searched and analyzed before the tax authority does so.

The Georgian court system in general always takes into consideration all the facts, while deciding the disputed case and based on the facts issues a decision.

Tbilisi City court stated that the main aim of article 73 (9)(B) of the Georgian Tax Code is that there is a reasoned assumption that parties of legal relationship chose a certain form of the legal relationship to avoid taxes and in reality, the taxable transaction has different substance.²⁹ Additionally, the Court stated that parties of legal relationship based on article 319 of Georgian Civil

²² *Kesteren H. V.*, Taxable and Non-Taxable Transactions, in: *Lang M., Pistone P., Rust A., Schuch J., Staringer C., Raponi D. (Eds.)*, Recent Developments in Value Added Tax, Vienna, 2016, 225.

²³ Art. 96, General Administrative Code of Georgia, LHG, 32(39), 15/07/1999.

²⁴ Decision of September 23, 2014 case № BS-246-243(K-13) of Supreme Court of Georgia.

²⁵ Ibid.

²⁶ Decision of February 18, 2014 case № BS-463-451(K-13) of Supreme Court of Georgia.

²⁷ Ibid.

²⁸ Art. 64, Tax Code of Georgia, LHG, 54, 12/10/2010.

²⁹ Decision of May 13, 2015 case № 3/7152-15 of Tbilisi City Court.

Code can choose any form of the legal relationship of their choice, as long as it is not illegal or against the law.³⁰

The Court declared that the tax authorities have the right to change the form of the taxable transaction if in process of tax inspection they find out that the form does not respond to the substance which is indicated in the contract.³¹ Additionally, it is of vital importance that the substance of the disputed legal relationship should be a different agreement for the Georgian Tax Code purposes.³²

The same reasoning has been applied by the Tbilisi Appeal Court in their decision³³, where the Court decided that changing the form and substance of the contract is only allowed if there is a divergence between the form and substance and the main reason for such divergences is avoiding taxes.

In the same case, the Supreme Court of Georgia in its decision³⁴ made very important notes. The Supreme Court share the ideas of the Tbilisi City Court and Tbilisi Appeal Court and additionally stated that when tax authority decides to change the form of the legal relationship, it should take into consideration the legislation which was applicable at the moment when the legal relationship was formed between parties.³⁵ In the case, a person gave the government property for free and instead received land which was considered as barter by the tax authority, but the Supreme Court of Georgia stated that by the time the contract was signed, the legislation did not include the exchange of the property and the changes were made later in the legislation, therefore, tax authorities while evaluating transactions should have considered that factor and therefore, should not have changed the form of the contract.³⁶

The decision creates a certain framework for the tax authorities while they exercise their discretion, indicating that any transaction should be evaluated not only from the tax legislation perspective but all the related law requirements should be taken into consideration and if certain prerequisites did not exist at the moment when the legal relationship was formed and it was added later, it could not create a strong foundation for changing the form of the contract

Even though the decision gives some clarity on what needs to be done to change the form of the transaction, several questions remain unanswered. What kind of test needs to be fulfilled to change the form of the contract and what requirements should be fulfilled is not clear.

Tbilisi City Court stated that in any case when tax authority uses article 73(9) and changes the form and substance of the contract, the burden of proof lies on the tax authority and they should provide all the facts and proofs which indicates that their activity was legit.³⁷ Furthermore, the Court stated that the tax authority is obliged to point out all the facts and legislation which gave them the

³⁰ Art. 319(1), Civil Code of Georgia, Parliamentary Gazette, 31, 24/07/1997.

³¹ Decision of May 13, 2015 case № 3/7152-15 of Tbilisi City Court.

³² Ibid.

³³ Decision of March 16, 2016 case № 3B/2026-15 of Tbilisi Appeal Court.

³⁴ Decision of July 18, 2018 case № BS-854-846(K-16) of Supreme Court of Georgia.

³⁵ Ibid.

³⁶ Ibid.

³⁷ Decision of March 13, 2015 case № 3/2173-14 of Tbilisi City Court.

possibility to change the form of the legal relationship.³⁸ Such distribution of the burden of proof derives from the Georgian Administrative Procedural Code and article 17(2) which indicates that any administrative body is obliged to prove that the administrative act they issued is legit.³⁹ In the same case Tbilisi Appeal Court stated that when the facts are sufficient to prove that the legal relationship and contract form is what the parties intended and the substance is in compliance with the form, tax authorities do not have right to change form according to the article 73(9) of the Georgian Tax Code.⁴⁰ The Supreme Court of Georgia on the same case declared that the substance must be examined not from the Georgian Tax Code perspective but from the legislation which is originally intended to regulate the legal relationship which was formed between parties and if the substance of the contract responds the requirements stated in the specific legislation tax authorities are not authorized to change the form of the contract.⁴¹

5. The Practice of Court of Justice of the European Union

Taking economic reality into consideration while examining tax law related relationship when the form of the contract does not respond substance is well-known for Court of Justice of European Union (hereinafter referred to as CJEU) CJEU's decision on a case “Her Majesty’s Commissioners of Revenue and Customs v Paul Newey”,⁴² declares what role does a contract play when deciding how the transaction should be taxed. Legal relationships and contracts generally respond to economic reality but there are some cases when those two elements do not collide.⁴³ Based on CJEU's practice, in order tax system to be fully functioning, the economic factor plays a decisive role.⁴⁴ Based on those arguments, the court decided that if the contractual terms do not respond to economic reality, the contract should be disregarded and the operation should be evaluated from the economic point of view.⁴⁵ CJEU points out that when it is clear that the contract has one aim to avoid taxes, economic factors give guidance to tax authorities on how to deal with the transaction. The Court emphasizes the fact that for stability legal relationships and contractual terms must be considered while deciding how the taxes should be levied, but only when it responds to economic reality.⁴⁶ The CJEU states that when the contract is used as a mechanism to avoid taxes, it should never be taken into account.⁴⁷ According to Court practice, it is very important for economic and law stability that the party has a legitimate

³⁸ Ibid.

³⁹ Art. 17(2), Administrative Procedural Code of Georgia, LHG, 39(46), 06/08/1999.

⁴⁰ Decision of April 27, 2016 case № 3B/634-15 of Tbilisi Appeal Court.

⁴¹ Decision of March 14, 2017 case № BS-702-595(2K-16) of Supreme Court of Georgia.

⁴² Case C-653/11, *Her Majesty’s Commissioners of Revenue and Customs v Paul Newey*, ECR [2013].

⁴³ Ibid, § 25.

⁴⁴ *Radeva Y.*, VAT Implications of Cancellation Charges: New Substance-over-Form Rule?, *International VAT Monitor*, Vol. 30, № 1, 2019, 14.

⁴⁵ Ibid.

⁴⁶ Case C-653/11, *Her Majesty’s Commissioners of Revenue and Customs v Paul Newey*, ECR [2013], §§ 43-45.

⁴⁷ *Kesteren H. V.*, Taxable and Non-Taxable Transactions, in: *Lang M., Pistone P., Rust A., Schuch J., Staringer C., Raponi D. (Eds.)*, *Recent Developments in Value Added Tax*, Vienna, 2016, 221.

expectation of what the outcome might be if they aim to avoid taxes and conduct contracts accordingly.⁴⁸ Therefore, when a taxpayer decides to use the legal relationship as a tool to avoid taxes, the future outcomes of such actions should be easily foreseen.⁴⁹

Additionally, it is very important to note that when the above-mentioned principle is being used, the comparison according to the CJEU's practice is what is “normal” and “standard” in everyday life.⁵⁰ For the best possible outcome, the contractual terms should be compared to what is “standard” in economic reality and the decision should be derived from those two factors.⁵¹

Therefore, disregarding contractual terms and using economic factors happens when the contractual terms only intend to avoid taxes.⁵²

Additionally, there are no other arguments from CJEU case law on how national courts of the European Union should change or accept the already changed form and substance of the contract.

It is of vital importance that the line is being drawn between what is tax avoidance and what is tax planning to use the best possible tax incentives.⁵³ Disregarding contractual terms and using economic reality is only justified if the court of tax authorities declare that a contract is being used for avoiding taxes.⁵⁴

If the taxpayer can choose one from several mechanisms which is the best possible tax regime for their business and this choice is not against legislation and the choice is deriving from the legislation itself, this cannot be considered as tax avoidance and it is tax planning. Therefore this can never become the foundation of changing form of the legal relationship.⁵⁵

The CJEU on case “Centros Ltd v Erhvervs- og Selskabsstyrelsen” declared that any member state has the right and obligation to control taxpayers' activities and discover whether or not the taxpayer is avoiding taxes.⁵⁶ But in every case, the national court is obliged to learn all the facts and decide whether the activities include tax avoidance purposes and compare it to incentives granted by the European or national legislation. The CJEU additionally stated that if the taxpayer's activity does not display tax avoidance reasons, the court should consider that the taxpayer is doing his/her business normally and the incentives are deriving from the tax planning, which indicates that in that case tax authorities or national courts do not have right to change form or substance of the contract.⁵⁷

⁴⁸ *Kesteren H. V.*, Taxable and Non-Taxable Transactions, in: *Lang M., Pistone P., Rust A., Schuch J., Staringer C., Raponi D. (Eds.)*, Recent Developments in Value Added Tax, Vienna, 2016, 226.

⁴⁹ *Ibid.*, 228.

⁵⁰ *Radeva Y.*, VAT Implications of Cancellation Charges: New Substance-over-Form Rule?, *International VAT Monitor*, Vol. 30, № 1, 2019, 14.

⁵¹ *Kesteren H. V.*, Taxable and Non-Taxable Transactions, in: *Lang M., Pistone P., Rust A., Schuch J., Staringer C., Raponi D. (Eds.)*, Recent Developments in Value Added Tax, Vienna, 2016, 231.

⁵² *Henkow O.*, Financial Activities in European VAT, A Theoretical and Legal Research of the European VAT System and the Actual and Preferred Treatment of Financial Activities, Netherlands, 2007, 60.

⁵³ *Doesum A. V., Kesteren H. V., Norden G.-J. V.*, Fundamentals of EU VAT Law, Netherlands, 2016, 123.

⁵⁴ *Terra B. J. M., Kajus J.*, Introduction to European VAT (Recast), Amsterdam, 2020, 128.

⁵⁵ Case C-212/97, *Centros Ltd v Erhvervs- og Selskabsstyrelsen*, ECR [1999].

⁵⁶ *Ibid.*, § 24.

⁵⁷ *Ibid.*, § 25.

6. Conclusion

Changing the form or substance of the legal relationship is a problematic issue in Georgia and European Union. Taking into consideration that the tax law-related relationships generally are based on the economic reality, it is very hard to draw the line when the tax authorities are allowed to change the form of the contract.⁵⁸

The fact that the burden of proof lies to the tax authorities according to Georgian Court practice should also be taken into consideration, which is the right outcome, as the tax authorities decide that the operation does not respond to its substance and therefore it should be changed. The burden of proof in such cases creates a framework for tax authorities, as they have to prove legal grounds for using such discretion.

For article 73(9) to be correctly implemented by the Georgian Tax authorities, it is crucial that all the factors are taken into consideration and every case is discussed individually, as a general answer to the question when article 73(9) is applicable is hard to get as every case is complex and has a lot of factors which might be decisive as nowadays there are many ways how business operations are conducted.

In doctrine and the practice of Georgian Courts and practice of CJEU indicates, the legal relationship must be examined in the light of the specific legislation which regulates the relationship between parties. Additionally, normal business practices must be learned and compared to the disputed case and after all these factors are thoroughly examined, the conclusions whether the form can be changed or not can be derived. This is the minimum standard that must be fulfilled.

How the future court practice will be developed regarding the issue is still to be seen, as there are many ongoing cases in the Courts of Georgia and there are no final decisions on that cases yet.

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⁵⁸ *Jespersen C. B.*, Intermediation of Insurance and financial Services in European VAT, Netherlands, 2011, 32.

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26. Decision of April 27, 2016 case № 3B/634-15 of Tbilisi Appeal Court.
27. Decision of May 13, 2015 case № 3/7152-15 of Tbilisi City Court.
28. Decision of March 13, 2015 case № 3/2173-14 of Tbilisi City Court.
29. Decision of September 23, 2014 case № BS-246-243(K-13) of Supreme Court of Georgia.
30. Decision of February 18, 2014 case № BS-463-451(K-13) of Supreme Court of Georgia.