

The Impact of the Threat of Criminal Penalties for Tax Evasion on the Activities of Small Business in Russian Federation

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Abstract—The development of small business has long been declared as one of the priorities in the reform of Russian economy. It is expected that this will solve a number of economic problems, from providing the flexibility of the economy and job creation, to overcoming its natural resource dependence. At the same time, the problem of excessive criminal prosecution of small enterprises certainly plays a significant role in deterring its development, since criminal repression affects the basic most important interests of the person. With this in mind, the authorities have repeatedly made statements about the need to limit cases of criminal prosecution of entrepreneurs by the only cases when it is absolutely necessary. However, these declarations differed from reality for a long time and the number of cases of criminal prosecution under "entrepreneurial" articles only grew from year to year. In this study, the reasons for this situation and the motivations of public authorities are clarified. It is established that the main motive of the authorities is the desire to use the threat of criminal prosecution as the simplest and most effective means of improving the performance of their work at the costs of business representatives, even at the cost of their bankruptcy and termination of activities. A particular civil servant is interested only in the indicators of his work, for which he is accountable and not the aims of state policy in the economic sphere. Moreover, representatives of small enterprises are the easiest target here, because they do not have sufficient administrative and financial resources to take advantage of qualified legal and economic assistance. It is established that to reverse the situation and shift the focus from the criminal legal methods of influence towards financial here helped only a radical change in legislation associated with an increase in the minimum amount of arrears needed for the act to be recognized as a criminal one. This gives basis to assert that in the future only such radical methods will be effective to reduce criminal-law pressure on business. In all other cases, criminal-law methods of influence on business continue to be the most simple and effective and therefore the most attractive for the state officials.

Keywords—*small enterprises; tax evasion; VAT; economic crimes; criminal prosecution; economic growth*

I. INTRODUCTION

In the last years, for quite a long period of time, officials have been making statements about the need to reform control and oversight activities in general [1] and reduce the number of cases of criminal prosecution for economic crimes in the business sphere in particular. It is expected that this will reduce the pressure on business from government agencies, which prevents the growth of small enterprises [2],

and will create a more favorable business environment [3]. This in turn will contribute to the development of entrepreneurship [4] and overcome the excessive state impact on small business [5].

Despite the fact that the issues under consideration are often quite actively discussed in the mass media and in the scientific literature, it is easy to notice that such a discussion is mainly limited to the analysis of individual cases, or concerns large and medium-sized enterprises. This is partly because these categories of business enterprises have greater access to the mass media, and partly because these enterprises are mainly able to use qualified economic and legal assistance, which today can be very expensive. Accordingly, it is these cases that become the subject of discussion in the professional environment and are further analyzed and summarized in scientific research. The activities of small enterprises in current conditions do not overlap with the activities of scientists and professionals who form the agenda in the relevant issues and discussions. A special study should be made that allow forming an idea of the problems arising in this field for small business.

The aim of this study is to assess the importance of the threat of criminal prosecution for economic crimes for the development of small enterprises in the Russian Federation.

II. MATERIALS AND METHODS

For the purpose of this study, small enterprises, as well as employees of state and law enforcement agencies working with them were interviewed.

The method of interviewing was chosen mainly because the questionnaire is associated with the study of already known issues and answers to pre-formulated questions. It is no secret that the columns of questionnaires, which are invited to freely express the respondent's opinion, usually remain blank. All the more so for the cases where the doctrinal norms are at odds with the practice of the behavior of persons pursuing their interests, and sometimes these norms are directly violated. This applies not only to business representatives, but also to representatives of public authorities who fear to put on paper the facts that they are quite ready to report in a private conversation during an interview.

The interviewing made it possible to assess not only the formal rules available in the relevant field, but also the informal rules and regulations that are emerging here, which,

sometimes, despite the liberalization of legislative provisions remain unchanged, or change very slightly [6] and continue to have a deterrent effect on the development of the economy in general and small business in particular.

Besides, the study used the doctrinal method: the analysis of legislation, the method of comparison of changes in practice of the subjects with previous changes in legislation.

III. RESULTS

At the first stage of the study it was found that the it is the criminal prosecution for tax crimes that is the most real threat for small enterprises [7]. The threat that criminal prosecution will be used as a means of unfair competition, the solution of economic and corporate dispute is much less likely. The competitors in small business usually do not have the "administrative resources" to organize such criminal prosecution. Accordingly, if attempts to resolve an economic dispute in this way are made, they usually result in a well-founded refusal to initiate criminal proceedings by law enforcement agencies, indicating that there is an economic dispute that must be resolved in civil proceedings.

At the same time, criminal prosecution for tax evasion, which is initiated during the on-site tax audit, is of great importance for the activities of a small enterprise. It often leads to the fact that the first on-site tax audit becomes the last for a small enterprise, after which its activities cease. For a small enterprise in criminal prosecution the greatest role is played by the possibility of imposing a criminal punishment [8], which largely depends on the judicial discretion [9]. It is not known in advance that makes the entrepreneur fear the worst.

In private conversations the inspectors of on-site inspections departments of the tax authorities often reported that one of their managers before the start of on-site tax audit set them the task to find the arrears of tax in the amount of not less than 2 000 000 rubles. This figure appeared not by chance. Prior to the amendment of the criminal law of 03.07.2016, tax evasion in the amount of more than 2 000 000 rubles provided grounds for criminal prosecution. At the same time, if the amount of arrears was less than 2 000 000 rubles, no other liability except for tax liability occurred. That is, the tax authorities during the on-site tax audit initially set the task of creating a threat of bringing the entrepreneur to criminal responsibility.

During the interview of the tax authorities' inspectors it was found that this situation is usually not caused by the desire to create conditions for corruption and illegal remuneration from the audited person, under the threat of criminal punishment. The reasons here are quite prosaic and lie in the formed internal criteria for assessing the effectiveness of the tax authorities, intricately intertwined with the provisions of tax and criminal legislation. So, one of the indicators here is the additional charge and collection of taxes on the basis of a tax audit. If an additionally charged tax amount does not allow to bring a person to criminal responsibility, but is very serious for a small business, it is likely that the entrepreneur will prefer to part with the business and will not repay it. This, in turn, increases the rate of uncollected tax debts, which is an extremely negative indicator showing the unsatisfactory work of the tax agencies. It is indicative that the interviewed inspectors of

on-site inspections departments clarify that they personally are not interested in the collection of the additional charged taxes. This is the problem of the tax debt collection department, so it does not touch them. However, for the top management of the tax agencies, which is responsible for working results of all departments, it is understandably a matter of interest. The taxes additionally charged, but not collected, increases the overdue debt, which is a negative indicator of the work of the tax agencies in general and its top management in particular. In this regard, the leaders set the task to their subordinates during the on-site inspections to achieve such amount of additionally charged taxes, which is sufficient to create a threat of criminal prosecution. As it guarantees that under the threat of criminal punishment the person will be compelled to pay this sum.

In turn, the entrepreneur, being under the threat of criminal prosecution, can not just go to bankruptcy of the business, which has been charged additional taxes. This actions will put the entrepreneur to the situation that he or she will be prosecuted under article 199 of the Russian Criminal Code as a natural person. In the result, he or she will be punished, and also tax debt of the small enterprise will be collected from him or her personally in damages caused by the crime. At the same time, the entrepreneur has another option. According to part 1 of article 76.1 of the Russian Criminal Code the natural person who has for the first time committed the crime covered by articles 198 - 199.1, 199.3, 199.4 of the Russian Criminal Code is exempted from criminal liability if the damage caused to the budget system of the Russian Federation as a result of the crime is compensated in full. That is, the entrepreneur can pay their tax arrears and he will be obligatory released from criminal liability. As a result, a person is faced with a choice of either to pay of arrears and exempt from criminal liability, or to get criminal punishment for tax evasion and to be made to pay the tax arrears. In such a situation, the choice is obvious and the entrepreneur is forced to repay the arrears, including through the personal funds not used in business.

Those who try to prove that the tax is added unreasonably and he or she didn't commit criminal act must be analyzed separately. Not only tax, but also law enforcement agencies treat them very negatively. Tax and law enforcement officials regard such a person almost like a personal enemy, who instead of quietly paying tries to fight them. Accordingly, any arguments and evidence of his or her innocence, which the person gives, are ignored and refuted often by very questionable methods.

Interviewing of entrepreneurs and tax authorities officials show that additional charging during the on-site tax audit is made mostly on the value added tax (VAT), which has long been the main budget-forming tax [10]. The mostly spread reason of additional charges on VAT is recognition as unjustified of VAT deductions declared by the entrepreneur. This is usually due to the fact that the counterparty who issued the invoice on the basis of which the deduction is made has not paid VAT to the budget. The deduction claimed on the basis of such invoice is deemed unjustified on various grounds. First of all, the argument about the fictitious nature of the business transaction is used here. The tax agency in the inspection certificate indicates that the supply of goods, works or services was not in fact, and the invoice was issued

for a non-existent transaction, entirely for the purpose of obtaining a VAT deduction.

Most entrepreneurs initially do not give due importance to such statements of the tax agencies. They believe that it is easy to prove the reality of the business, because they produced products out of the raw materials or sold the purchased goods and showed the sale of goods or manufactured products as a basis for VAT. They believe that if there was a sale of goods, then there must be its purchase, and the reality of the purchase of goods is confirmed by the fact of sale of goods. This confidence is often reinforced by judgment on similar cases available in the Internet, where the taxpayer has been able to prove the validity of the tax deduction. In this case, the entrepreneur often misses the fact that per one such positive decision there are many thousands of negative ones. After that, the entrepreneur discovers that the invoice for the purchase of goods, which is the basis for the declaration of tax deduction, is excluded, but the invoice for the sale of the same goods or products, made of them, which is the basis to charge the tax, no one is going to exclude. This usually causes confusion and is perceived as extreme injustice. After that, the entrepreneur begins to provide evidence of the reality of the transaction. Among entrepreneurs, it is widely believed that this requires video recording of receipt and unloading of goods, as well as the transmission of shipping documents and invoices. Some of them, according to their statements, even install video cameras for this purpose and organize permanent video recording in their offices and warehouses.

If the entrepreneur finally was able to prove the reality of the business transaction, then the second argument of the tax agencies comes into effect that the entrepreneur imprudently chose the counterparty who issued him or her an invoice, without reflecting it in the accounting and without paying VAT to the budget. Initially, the entrepreneur thinks that a proof of sufficient prudence in business transactions is the fact that he or she took from the counterparty the documents provided by the law, and the entrepreneur should not be responsible for another person. However, very soon the entrepreneur discovers that the design of sufficient prudence is put into practice precisely in order to introduce such a responsibility and here the judgment in favor of the entrepreneur is quite rare. The argument is simple: once the counterparty has not paid, then sufficient prudence is not shown. Thus, as a bonus for the proof of the reality of the business transaction the entrepreneur will most likely avoid criminal liability, because lack of prudence is not intent, but he or she will still pay the additionally charged tax arrears.

Thus, as a result of all the efforts and plenty of time and money spent, a person comes to what he or she could get from the very beginning, namely to pay the arrears and get exemption from liability.

Most of the entrepreneurs we interviewed, who tried to prove their innocence and not to pay additionally charged tax arrears, being people who are able to fairly soberly and objectively assess the situation, at a certain stage refused this idea and went to pay the additionally charged tax arrears with the subsequent termination of the criminal case on the basis of part 1 of article 76.1 of the Russian Criminal Code.

Federal law No. 325-FZ of 03.07.2016 "On amendments to the Criminal Code of the Russian Federation and the Code

of Criminal Procedure of the Russian Federation" increased the minimum amount of tax arrears sufficient for criminal prosecution to 5,000,000 rubles. The increase in two and a half times here should be recognized as very substantial, especially given the fact that we are talking about small businesses. This increase contributed to the fact that there have been significant changes in the practice of tax and law enforcement agencies with small businesses. More than two years have passed since the increase in the minimum of tax arrears for criminal prosecution. This is a fairly long period, which allows us to talk about the sustainability of the changes. First of all, the top management of the tax agencies tried to raise up to 5 000 rubles the "standard" of additional charges of taxes for inspectors carrying out on-site tax audits. However, in many cases it is impossible to reach such an amount of additional tax charges due to objective reasons. If we are dealing with a small enterprise, the turnover of the organization often does not allow to charge this amount of tax. Even if all tax deductions declared by the small enterprise recognized to be unjustified, it would not be sufficient to achieve a minimum, needed for criminal liability. Besides, such a conclusion of the tax audit will look more than strange. This led to a very significant change in the working methods of tax agencies with small businesses and to a significant reduction in the threat to the entrepreneurs to be subjected to criminal penalties for tax evasion. Concurrently tax agencies radically changed approaches to the organization of tax audit as initially the most conflict procedure in interaction with taxpayers [11] and began to develop control over the real-time reflection of invoices in the accounting. The entrepreneur learns that the counterparty who issued the invoice to him or her did not reflect it in accounting or did not pay VAT, not in a few years during the on-site tax audit, when such transactions have accumulated quite a lot, but in a few months, when the amount of arrears is not very large and can be paid and the entrepreneur can stop working with this counterparty in time.

IV. CONCLUSION

Due to this change in legislation and practice, the threat of criminal prosecution for tax evasion has significantly decreased for the majority of entrepreneurs we interviewed. This distinguishes the above mentioned amendment of the criminal law from previous reforms, the effectiveness of which was generally very limited [12]. The problem of blocking accounts by a bank or a tax agencies is already considered by many entrepreneurs as more urgent. This effect of the amendment of the criminal law, which increased the minimum amount of tax arrears for criminal prosecution, should be recognized as positive. This has finally made it possible to change the situation with the artificial criminalization of small business [13], to move to a balanced approach of its decriminalization [14], to reduce significantly the threat of criminal punishment for tax evasion for entrepreneurs in small business and to shift the emphasis towards softer economic measures within the tax legislation. This approach, along with reduction of the tax burden on small businesses [15], should be one of the conditions for its sustainable development.

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