



Russian Tax Newsletter

June 2017

Important Recent Tax Changes

Russian Federal Tax Service (FTS) Drafts Revised Country Blacklist

The FTS has issued a draft order pursuant to which, starting from 1 January 2018, BVI and the Republic of Korea will be removed from the blacklist of countries not sharing tax information. The draft blacklist comprises 108 countries and 18 territories.

In compiling this list, the FTS considers not only the existence of a formal data exchange agreement, but also whether such exchange is actually possible, as well as any negative experience with the country tax authorities (Letter of the Ministry of Finance of the Russian Federation dated 07.10.15 No. 03-08-05/57368).

Therefore, indirectly the removal of BVI from the blacklist could mean that the FTS has obtained information meeting the relevant requirements for quality, completeness and responsiveness from BVI government authorities.

<http://www.rbc.ru/rbcfreenews/595b1f359a79475d2300d912>

Russian Federal Tax Service to Create Online Service to Identify Shell Companies

The FTS will be creating the online service to assist taxpayers in identifying which of their counter-parties could be shell companies. The service will be based on tax ratings to be assigned to each economic entity. By using these ratings in selecting business partners, an entrepreneur could reduce the risk of additional taxes solely because their counterparty is treated as a shell company.

http://taxpravo.ru/novosti/statya-393189-fns_predostavit_nalogoplatetschikam_instrument_dlya_vviyavleniya_partnerov_odnodnevok

Russian Duma Passes (Second Reading) Legislation Incorporating the Concept of Unjustified Tax Benefit

The draft legislation proposes a new approach to determining when taxpayers are improperly reducing their tax liabilities. The legislation states that a reduction in tax liabilities is improper if accomplished by misstating accounting or reporting or by ignoring the crucial tax doctrine – “priority of substance over form”.

In addition, the legislation states that non-payment of taxes by a taxpayer’s counterparty, some immaterial defects in compiling documents or the possibility of structuring a business or transaction differently (but with a greater resulting tax) are not be treated as separate

grounds for refusing deductions or expenses, if there are no other indications that a business transaction should not be respected. The draft legislation provides that the FTS, by exercising tax control, bears the burden of proof that a reduction in tax liabilities by a taxpayer was unjustified.

Draft law No. 529775-6 “On making amendments to Part One of the Russian Tax Code” (re: establishing limits for taxpayers in respect of exercising their rights and performing their obligations):

[http://asozd2.duma.gov.ru/main.nsf/\(SpravkaNew\)?OpenAgent&RN=529775-6&02](http://asozd2.duma.gov.ru/main.nsf/(SpravkaNew)?OpenAgent&RN=529775-6&02)

Review of International Law

Multilateral Convention on Taking Measures Related to Tax Agreements to Combat Base Erosion and Profit Shifting (MLI) was Signed

On 7 June, the signing ceremony was held for the Multilateral Convention on Taking Measures Related to Tax Agreements to in order to Combat Base Erosion and Profit Shifting (MLI): <http://www.oecd.org/tax/treaties/beps-mli-position-russia.pdf>

MLI's Key Provisions:

Anti-Avoidance Provisions

A DTT will contain a special provision to counteract abuses in applying DTTs, the so-called principal purpose test (PPT test), pursuant to which, if one of the principal purposes of any structure or transaction is to avoid any tax, then the relevant provisions of the DTT will not apply.

Based on the MLI signatories, the PPT test is expected to be applied to DTTs with Russia, including Cyprus, the Netherlands and Luxembourg. In practice this means that, notwithstanding the lack of specific limitation of benefits provisions in a DTT, the ability to benefit from a DTT could be complicated and will require a real business purpose for creating the structure or for entering into the transaction.

Dividend Taxation

Preferential rates of withholding tax on dividends will only apply if a person or company is the beneficial owner of the dividends and owns/exercises control for at least 365 days over the necessary amount of capital/shares/participatory interest required under the DTT to qualify for such benefits. Such conditions for lower withholding rates on dividends will apply to the DTTs with Cyprus, Hong Kong, Luxembourg, the Netherlands, Singapore, Switzerland, among others.

Sales of Shares (a Participatory Interest) of a Real Property Company

Any income from the sale of shares (or a participatory interest) of a Russian company, the assets of which consist of more than 50% real estate located in the Russian Federation, is subject to tax in Russia, notwithstanding the fact that the relevant DTT generally exempts gain from the sale of shares from tax in Russia. This provision will apply, if, pursuant to the MLI, a DTT signatory announces its intention to follow this approach.

For example, the DTTs with the Netherlands, Singapore and Austria now exempt gain from the sale of a real property company shares (participation interest) from tax (in respect

of Singapore, the criterion is “consist of more than 75% real estate” instead of 50%). The current approach of the DTTs will continue to apply, i.e. such exemption will still be available, provided that the anti-avoidance (PPT and other conditions specified above in MLI) are met.

Mutual Agreement Procedure

A taxpayers can request a competent authority proceeding by the countries which are signatories to a DTT in order to initiate a mutual agreement procedure. If a taxpayer believes that such competent authority proceeding applied a DTT provision incorrectly, the taxpayer has three years from the date of the challenged incorrect application of the DTT in which to initiate such claim.

This provision is mandatory for all MLI signatories (the so-called “minimum standard”) and applies without any exception.

Other Provisions

MLI also introduces the following provisions targeted at preventing DTT abuses:

- introduction of special rules to combat the use of hybrid instruments and structures, persons with double tax residence, tax transparent structures; and
- rules to prevent “artificial” avoidance of a permanent establishment (in particular, by means of agency agreements, special types of activity, division of contracts).

Therefore, we recommend:

- performing a comprehensive analysis of the “sustainability” of a given structure under the MLI, subject to the position of the tax authorities in the countries where the business is conducted;
- considering and implementing an action plan to minimise the risks identified prior to MLI introduction; and
- monitoring the positions of MLI signatories until finally approved.

OECD Published Draft Documents Related to BEPS:

- updated draft of additional guidelines for determining the profit of a permanent establishment (including examples where a permanent establishment was created as a result of intermediary sale and purchase agreements and dividing the business activity among various jurisdictions); and
- updated draft of transfer pricing guidelines on application of the profit split method.

The Draft documents are subject to public comment until 15 September 2017:

<http://www.oecd.org/tax/oecd-releases-beps-discussion-drafts-on-attribution-of-profits-to-permanent-establishments-and-transactional-profit-splits.htm>

More Signatories to the Multilateral Competent Authority Agreement on the Exchange of CbC Reports

The following countries on 22 June signed the Multilateral Competent Authority Agreement on the Exchange of CbC Reports (CbC MCAA): Belize, the Cayman Islands, Columbia, Haiti, Pakistan, Singapore, as well as Turks and Caicos Islands.

Singapore also signed the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Account Information (CRS MCAA): <http://www.oecd.org/tax/third-meeting-of-the-inclusive-framework-on-beps-delivers-results.htm>

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