

VAT Exemption as Part of the Tax Maneuver in the IT Sector

July 2020



Draft law

On 21 July 2020 the State Duma adopted a draft law on “tax maneuver” in the IT sector in the first reading¹. The draft law has been prepared further to the orders of the President of the Russian Federation on support for the digital technologies sector. The second reading of the draft law is scheduled for 22 July 2020. The draft law stipulates, inter alia, a change in the procedure for applying the VAT exemption (for more details about the draft law and all the tax support measures for the IT sector, see the Alert on KPMG’s website).



What is changing?

Currently VAT exemption applies to the sale of exclusive rights to software and databases (hereinafter “Software”), and rights to use them based on a license agreement.

The draft law stipulates the following amendments:

- The VAT exemption will apply to Software that has been included in the Unified Register of Russian Programs for Computers and Databases (hereinafter the “Register”);
- The VAT exemption will apply to the sale of rights to use the indicated Software (including updates and additional functionality) through the remote online access;
- The VAT exemption will not apply if the “rights to use Software consist of the receipt of an opportunity to disseminate advertising information in the Internet and/or receive access to it, post offers on the acquisition (sale) of goods (work, services), property rights in the Internet, look for information on potential buyers (sellers) and/or conclude transactions” (hereinafter “Advertising Software”).

These amendments may enter into force from 1 January 2021.

¹<https://sozd.duma.gov.ru/bill/990337-7>



What are the anticipated consequences for business?

If adopted in its current version, the draft law would have the following consequences for business:

Russian companies:

Software included in the Register:

- The provision of exclusive rights and rights to use Software under a license agreement will be still VAT exempt, with the exception of “Advertising Software”.
- The draft law also aims to resolve the issue of applying the VAT exemption to companies providing “cloud” Software as a service (based on the “SaaS – Software as a service” model), Software updates and additional functionality.
- Companies providing “Advertising Software” will have to change their approach and charge VAT (even if the rights to the “Advertising Software” are transferred under a license agreement). Russian companies acquiring such “Advertising Software” should be eligible to recover such VAT if the Software is acquired for VATable activity.
- The amendments would result in additional VAT costs in case of the sales of “Advertising Software” to individuals and Russian companies which use the Software in VAT exempt supplies (for example, banks, insurance companies).

Software not included in the Register:

- In most cases, the provision of Software between Russian companies should not result in additional VAT costs: Russian companies selling the Software will charge VAT at the 20% rate while Russian companies acquiring the Software will be entitled to recover such VAT (if the Software is acquired for VATable activity).
- Russian companies selling the Software to foreign customers should not charge VAT (as the place of supply of the Software is not deemed to be Russia). At the same time, however, these Russian companies should be eligible to recover VAT incurred on the development of the Software and other expenses related to such Software.

Foreign companies:

- The sale of Software by foreign suppliers to Russian customers should be subject to VAT. In most cases the foreign suppliers of Software are registered with the Russian tax authorities (due to the provision of electronic services). Such suppliers should start charging and paying VAT in Russia on the sale of Software to the Russian customers. The Russian customers of the Software should be eligible to recover input VAT if the Software is acquired for VATable activity.
- Additional VAT costs will arise in case of the sale of the Software to certain categories of companies (for example, banks, insurance and healthcare companies), SMEs applying special tax regimes, and individuals.



What to do?

It may be advisable for companies operating in the IT sector as well as companies from other industries acquiring the Software to take the following actions:

- to identify the Software included in the Register and assess whether it is possible to include in the Register the Software, which is not currently included there, to apply the VAT exemption;
- to identify types of the Software which would be classified as “Advertising Software” and would be subject to VAT;
- to analyze the possibility to apply the VAT exemption to the “cloud” Software and services which are currently subject to VAT, inter alia, determine the type of agreement under which the Software should be transferred, what should be treated as VAT exempt updates and additional functionality, etc.;
- to analyze current license agreements and other agreements which are the basis for the provision of the Software (for example, service agreements, offers, terms of use of the Software and online services), and assess whether amendments need to be introduced to them in order to apply the VAT exemption or to charge VAT;

- to agree with counterparties on the approach to determine the fee under license agreements and other agreements on the provision of the Software and whether the fee will be increased by the amount of VAT, and introduce amendments to agreements where necessary;
- to implement changes to accounting systems and the documents (in particular, foreign software suppliers registered with the Russian tax authorities as electronic service providers will have to issue invoices which meet the requirements of Russian legislation so that Russian customers could recover VAT);
- to ensure the changes in calculations for the purposes of input VAT allocation and separate accounting between VATable and non-VATable activities, and check that the documents required for VAT recovery or refund are in place.

Professionals from KPMG’s Indirect Tax Practice would be delighted to discuss any issues and consequences relevant to your business due to the legislative amendments in question.

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