Osteuropa kompakt
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Azerbaijan

Amendments to the Law on Labour Pensions

Amendments eliminate the concept of "basic part of the labour pension" and the 12 year work experience required for the appointment of pension. It also increases the retirement age for women and men to 65 years.

Due to elimination of “base part of pension” concept, amendments introduce the concept of “minimum pension”, which is equal to 110 AZN.

According to the amendments, the length of work experience required for retirement for members of all professions have been increased, with the exception of police and military personnel.

Another change covers the transfer to the individual account of a citizen of a bigger part of the paid contributions for compulsory state social insurance. Ninety percent of the contributions paid by a citizen on compulsory state social insurance will now be reflected in his/her account.

The regulations for non-performing (toxic) assets

These regulations are one of the important steps of the implementation of Strategic Road Map on the development of financial services. According to the new Regulations, the non-performing (toxic) assets are pledged assets in line with the regulatory acts of Financial Markets Supervision Chamber.

The opinion of Financial Markets Supervision Chamber on the assets considered toxic by the bank should be obtained 20 days prior to submission of these toxic assets.

Also, the Regulations indicate minimum requirements of contract submission on non-performing assets (for example, the contract should include amount, parties rights, obligations, etc.)

In addition, the Regulations have been prepared in line with article 164.1.36 of the Tax Code. According to this clause, submission of non-performing (toxic) assets are implemented from 1 January 2017, for a 3 year period.

Amendments to the Law on Currency Regulation

The amendments introduce rules on obtaining license for currency exchange activity, which defined as acquisition, sell and change of foreign currency in Azerbaijan and can only be performed in form of cash and upon clients' request.

Resident legal entities and individuals, as well as branches of non-resident legal entities, willing to engage in currency exchange activity will need to file an application for obtaining license and submit a package of documents to the Financial Markets Supervision Chamber ("FMSC"), and also place security deposits in the following amounts to certain banks:

- AZN 50,000 and USD 50,000 in Baku;

- AZN 25,000 and USD 25,000 in Sumgayit and Absheron districts;

- AZN 10,000 and USD 10,000 in Ganja.

The response to this application shall be given within 20 days after its submission to the FMSC. License for the performance of currency exchange activity is termless.

The FMSC will determine rules and territory of currency exchange operations.

Changes to the Tax Code

The Law on Changes to the Tax Code, dated 14 April 2017, introduced several amendments to article 58.7-1 of the Tax Code.

According to new changes, taxpayers are subject to financial sanctions for failure to conduct below listed operations cashless, i.e. for receiving in cash:

- Receipt of money by leasing providers and loan issuers;
- Payment of insurance payments and receipt of insurance premiums by insurer or reinsurer;
- Receipt of service fees and other levies by state authorities, state entities, budgetary organisations and public entities;
- Receipt of stationary phone charges and utilities;
- Receipt of tuition fees;
- Receipt of fees for tourism agency services.

Furthermore, taxpayers are also subject to financial sanctions for failure to conduct below listed operations cashless, i.e. for paying in cash:

- Any payments over AZN 30,000 per calendar month by VAT payers and/or by taxpayers engaged in trade and (or) public catering whose taxable turnover exceed AZN 200,000 in any 12 month period;
- Any payments over AZN 15,000 per calendar month by other taxpayers;
- Payment of salary and other relevant compensations to employees;
- Any payments out of funds earned from state procurement contracts.

The amount of applicable financial sanctions depends on the number of violations in a calendar year and includes below percentages of all operations involving violation of the Law:

- 10% - one violation in a calendar year;
- 20% - two violations in a calendar year;
- 40% - three or more times in a calendar year.

Note: This requirement is not applicable to those engaged in retail trading, public catering and service industry whose taxable supply are below AZN 200,000 in any month (months) of a consecutive 12 month period.

Amendments to the Law on Central Bank

Amendments terminate the article of the law regulating extension of targeted loans funding socio-economic projects and supporting real sector of economy, built on the state guarantee. Amendment also eliminates the clause of the law enabling Central Bank to acquire securities issued by the state to cover targeted loan commitment.

Amendments to the Code of Administrative Offences

Amendments set fines for the following offences:

1. Operation and administration of a ship with discrepancies that violate maritime security and contradict to requirements of international conventions and executive authorities;
2. Activity of sea ports without the documents listed in “The International Ship and Port Facility Security Code”;
3. Appointment of persons not holding the relevant license for performing the activities in a ship requiring license under “The International Convention on Standards of Training, Certification and Watch keeping”.

Amendments to the Criminal Code

According to amendments, violation of the rules for allocation of land plots for construction by officials will cause criminal liability. Previously violation of these rules was subject to administrative liability. The liability for violation of these rules varies from two years of corrective works and deprivation of right to hold certain positions and engage in certain activities to imprisonment up to eight years.

Draft law on amendments to the Labor Code

According to the proposed amendments, terminating an employment agreements due to staff reductions, employer will need to take the experience of an employee into consideration. In case if an employee has less than one year experience, the notification regarding the termination of employment agreement should be sent to him/her at least 2 weeks in advance, employees having an experience between one and five years should be notified 4 weeks in advance, while employees having experience between one and ten years should be notified about the termination of their employment agreements at least nine weeks in advance.

The experience of an employee should also be considered when calculating compensation and when calculating the amount of salary to be paid instead of notifying an employee about upcoming staff reductions (according to the Labor Code, employer may pay an employee amount of money not less than his/her average monthly salary, instead of notifying an employee about employment agreement termination in advance).

This alert is based on a draft law. We will monitor it and update information once the draft law is adopted.

Amendments to the Law on State Duties

According to the amendments, state duty in the amount of AZN 20 has been set for obtaining certificates of compliance of goods (services and work), process, management system and staff with requirements defined by standards, technical regulations and legal acts.

Agency certifying compliance (an agency holding a relevant licence to conduct compliance evaluations) should also pay the state duty in the amount of AZN 20 for getting certificate on accreditation.

The Action plan on improvement of Business Environment

President of the Republic of Azerbaijan approved the action Plan on Improving Expediency of Business Environment in Azerbaijan and improving position of the state in international ratings. The action plan covers following areas:

- The development of financial markets and the availability of loans;
- Effective governance and macro-economic indicators;
- Labour market;
- Physical infrastructure;
- The execution of contracts, dispute resolution, closure and bankruptcy of the enterprise, the judicial system and rule of law;
- Corporate governance, investments, investors' interests;
- Foreign trade and trade tariffs;
- Human capital;
- Efficiency of commodity market and competition;
- Technologies and innovations;
- Tax and accountability;
- Border trade;
- Healthcare system;
- Connection to the power supply network;
- Obtainment of construction permits; - Corruption and transparency;
- Property registration;
- The costs associated with the fight against crime.

The Commission on Increasing Expediency of the Business Environment has been assigned responsible to coordinate the execution of the action plan.

Draft Law on Amendments to the Labour Code

The draft law covered in PwC Azerbaijan Times Issue#18 has passed the first hearing at Milli Mejlis.

The following changes have been approved during the first hearing:

- Fixed term employment agreements may be signed for any term determined by mutual agreement of the parties. Previously this term was limited to 5 years.
- Amount of termination benefits paid to employees in case of termination of the employment agreement by employer's initiative (liquidation of the entity and redundancies) and notification period, as well as amount compensation instead of notification period, will vary depending on seniority (experience) of the employee within that entity.

Seniority	Minimum amount of termination benefit equal to	Minimum period of notification	Compensation instead of notification
Up to a year	Average monthly salary	Two weeks in advance	0.5 of the average monthly salary
From one to five years	1.4 of the average monthly salary	Four weeks in advance	0.9 of the average monthly salary
From five to ten years	1.7 of the average monthly salary	Six weeks in advance	1.4 of the average monthly salary
More than ten years	Double of the average monthly salary	Nine weeks in advance	Double of the average monthly salary

Decree on acceleration of creation of free trade zones

President of the Republic of Azerbaijan established a working group responsible for acceleration of creation of free trade zone in Alat settlement of Garadagh district in Baku. The working group has been instructed to analyse existing draft law on creation of free trade zones and to present a final version of the document, which will reflect interests of the state and investors.

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Latvia

Various levels of process efficiency

In an earlier edition of Flash News we wrote about the three main reasons that hinder process efficiency improvements: lack of clarity about goals and how to achieve them, staff resistance to change, and inability to achieve efficiency in the long term. This article takes a look at potential solutions to these problems.

Recipes for implementing process efficiency projects successfully

There are a number of ways to make your processes efficient. All you need to do is choose the method and approach (e.g. Lean, Kaizen, Six Sigma, 5S) that is best suited for your situation, and put together a results-oriented team, set up a performance monitoring system, make practical changes to your processes, use appropriate ICT support etc.

Implementing changes

Changes can be implemented by taking ten steps. These steps and their goals are described in the table below:

Step	Goal
Define your vision	Start and keep up efficient planning that ensures you will achieve your main organisational goals. We often see in practice that a plan is understood to mean just a timetable. For efficiency projects, however, a benefit management plan is crucial (i.e. one that shows what qualitative and quantitative benefits the project will bring).
Set up information centres	Understand what your information sources are and where you can obtain the necessary data to carry out a proper analysis. Such information centres are your corporate information systems, procedure descriptions, customer surveys, various statistics etc.
Hold planning meetings/ monitor performance	Start daily meetings and run training courses for managers about their content, style, approach and staff/team management methods. Everyone knows that if any change is to be implemented successfully, it must be discussed with and accepted by your staff. For this purpose it's very important to build a structured communication approach.
Implement visual management	Set up, streamline and involve staff in visual management on each site. Your staff should know how far you are on your way to your goal. Simple solutions do the job, e.g. information posted on a noticeboard or on the intranet.

Adopt a daily/weekly routine and practice	Analyse your operations and identify issues on each site. How is time being spent? Does that add value? If your company operates a timesheet system where staff record hours spent on activities, this is very helpful in planning for changes. Without such a system, you should think of some other methods, e.g. time monitoring, self-assessment questionnaires.
Adopt a common approach to analysis	Adopting mandatory business procedures, including meeting minutes and customer details, process mapping, RACI etc. It's especially important that you define such a common approach to analysis standards on large projects served by multiple teams. Without a common approach, it's difficult to steer the project towards a common goal.
Celebrate success	An approach that motivates staff and managers by recognising good results and hard work. Celebrate your successes, however small they might be, such as completed stages of a project, as that will inspire your team to carry on and complete the whole project successfully.

Core principles of Estonian corporate tax system

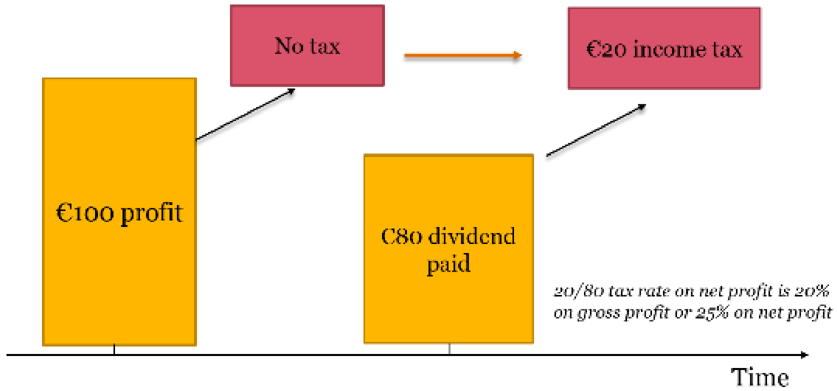
The Latvian Cabinet of Ministers' decision of 9 May 2017 to support the draft national tax policies for 2018–2021 has made it clear that the next six months will see significant changes to the Latvian tax system. Confirming the intention announced earlier to move the Latvian corporate income tax (CIT) regime closer to the Estonian model, the proposed policy solutions provide for reforming the CIT system from 1 January 2018 to charge a 0% tax on reinvested profits and a 20% tax on gross profits at the time of distribution. With the proposals still at a developmental stage, this article explores the Estonian model to discover how the so-called 20/80 tax rate principle works.

The 20/80 tax rate principle

With the implementation of its CIT reform in 2000, Estonia started a unique tax policy based on the main principle of not charging tax until profits are distributed to encourage long-term investment in companies and promote economic growth. The Estonian regime gives a full CIT exemption on undistributed profits (including income from business activities and company share sales as well as passive income such as dividends, interest and royalties). The mass media often call it the "0% reinvested profit model."

At the same time, the CIT calculation principle requires that the 20/80 rate be applied to the net amount of distributable profit, i.e. 20% on gross profit or 25% on net profit. To understand how the 20/80 principle works, let's look at a practical example.

A company reports a profit of €100 for the year. €80 is available for a dividend payment, and €20 must be paid in tax at the time of profit distribution:



Although technically the gross profit for the year (€100) attracts a 20% tax, the actual tax on the net profit received (€80) is 25% (€20 = 80 x 25%).

Tax compliance

While this calculation may initially seem complicated, Estonian taxpayers stress the simplicity of this system. According to PwC's 2016 Paying Taxes survey, the Estonian taxpayer annually spends an average of 81 hours on tax compliance. This ranks Estonia fourth among the EEA countries whose tax regime creates one of the lowest administrative burdens in Europe.

Administering the Estonian tax regime is based on the following calculation principles:

- Accounting profit doesn't need adjusting for tax purposes because there are no capital allowances, taxes losses or any other taxable income adjustments;
- Tax is charged on profits distributed in the tax period, including dividends (and surplus assets on winding-up), equity reduction payments or share repurchase, transfer pricing adjustments, taxable gifts, donations etc;
- The 20/80 tax rate applies to all non-business expenses that aren't eligible for a tax deduction (such as fines, securities purchased from tax-haven entities, staff and client entertainment expenses, and so-called representation expenses over and above a certain threshold);
- The tax period is one calendar month.

The reinvested profit regime outlined in this article applies to Estonian tax residents: Estonian-registered entities and permanent establishments. Certain structures such as pension funds and investment funds attract a special tax regime based on different principles from those described above.

New amendments to VAT Act take effect from 1 June

New amendments to the VAT Act were published on 10 May, which Parliament had been debating since October 2016 but didn't pass until 20 April 2017. The amendments come into force on 1 June, except for those relating to the direct application of zero-rating to supplies of goods and services to Allied Headquarters staff members and US diplomats, which come into force on 1 January 2018. This article explores what we see as key changes.

Input tax deduction point

Input tax is currently deductible only in one specified tax period when the criteria set by section 97(1) of the VAT Act are satisfied:

1. goods or services and a tax invoice have been received, or

2. a consideration for the supply of goods or services is paid before they are received.

This clause as amended allows a taxable person to deduct input tax on goods or services in the tax period when these conditions are satisfied or the following tax period.

For example, on 8 June Gem SIA receives goods from another Latvian-registered taxable person for making taxable supplies, and a tax invoice is issued on 5 June. The input tax appearing on the tax invoice can be reported by Gem SIA on its VAT return for June or July, assuming its tax period is one month. If it's one quarter, the input tax should be reported on the VAT return for the second or the third quarter.

Input tax adjustment for bad debts

Very important amendments have been made to section 105 of the VAT Act, which prescribes input tax adjustments for bad debts with respect to age limitation. This section now has a new subsection (2.1) stating that the three-year condition will be treated as satisfied if within three years after the debt arose –

1. a court claim has been filed to recover the debt from the customer – with respect to the case mentioned in section 105(3), i.e. the debt is €430 or more;

2. the customer has gone into bankruptcy – with respect to the case mentioned in section 105(4); or

3. the customer has gone into insolvency – with respect to the case mentioned in section 105(5).

This will solve the problem taxpayers faced where debt recovery or insolvency proceedings lasted longer than three years.

Construction services and alignment of terminology

Since the terms used in the VAT Act with respect to dealings in real estate, including construction services, aren't consistent with the terms used in the Construction Act (effective from 1 October 2014), the amendments substitute the term "renewal" for "renovation" and the term "rebuilding" for "reconstruction" throughout the Act. Paragraph 3 ("Zero Cycle Development") has been deleted from section 142(4) of the VAT Act to make it consistent with Cabinet Regulation No. 500, General Construction Rules, because they don't use such a term.

Section 142(1) of the VAT Act, which lists the services attracting reverse-charge VAT, has been amended to read as follows: "For the purposes of this section, construction services shall mean the performance of construction work for the erection of a new building (or engineering structure) or for the renovation, simplified renovation, reconstruction, restauration, conservation or dismantling of an existing building or its part, and all types of design work included in a contract for construction services."

Unfortunately it appears that Parliament hasn't supported the version of this clause proposed by the Ministry of Economy (MOE), which provided for applying reverse-charge VAT to "…the performance of any construction work and all types of design work included in a contract for construction services."

The MOE believes that section 142(1) refers to any type of construction work and design work: "…this broad coverage isn't altered by the separate reference to simplified construction processes. It was essentially construction work that was carried out as part of these simplified construction processes. The fact that renovation (renewal) and reconstruction (rebuilding) could in certain cases be carried out using a simplified construction process doesn't alter the fact that renovation or reconstruction was carried out. Depending on the type of proposed construction work and the type of the building (or engineering structure), the current construction rules provide for various types of construction processes and specify cases where the person requires no permit of any type. Yet this doesn't alter the fact that construction work of a particular type is carried out in all cases. Section 1 of the Construction Act names the types of construction work: renovation, installation, conservation, dismantling, placement, rebuilding, and restauration. Additionally, the building legislation uses the term "new construction" to indicate the creation of a new structure (one that didn't exist before). All the types of construction work mentioned above are covered by the umbrella term "construction work" in section 1(2) of the Construction Act."

In our opinion, had the MOE proposal been adopted, the tax authorities and taxpayers would better understand this clause and avoid disputes over interpretation.

Other amendments

The following amendments have also been made to the VAT Act:

Zero-rating will apply directly to domestic supplies of goods and services to staff members of an Allied Headquarters recognised in Latvia and their dependants, as well as domestic fuel supplies to the US Embassy in Latvia and its diplomatic and consular agents and support staff (from 1 January 2018);

With respect to the new Customs Code, the terms used in the VAT Act have been clarified, and non-residents will have more opportunities to stay unregistered for Latvian VAT;

An exemption will cover gambling games and lotteries organised through electronic communication services.

FTT affirms HMRC's refusal of VAT refund under Thirteenth VAT Directive

On 20 April 2017 the First-tier Tribunal (FTT) issued a ruling in JDI International Leasing Ltd vs HM Revenue and Customs. This case involves a claim by JDI International Leasing Ltd for VAT incurred in the UK when it acquired specialised tools for use on oilfields in the UK. JDI International Leasing Ltd ("JDI") is a company established in the Cayman Islands and has no fixed establishment in the UK. JDI wanted to recover the VAT under the Thirteenth VAT Directive (Council Directive 86/560/EEC) and made a claim under the VAT Act. HMRC refused the claim on the grounds that JDI made no use of the tools for an economic activity.

Background

JDI is a trader established outside the EU and a member of the Baker Hughes group of companies. JDI leased and then bought tools from a UK VAT-registered trader and was charged VAT on those transactions. JDI then leased the tools to Baker Hughes Nederland BV, a trader established in the Netherlands, for no consideration. JDI also sells spare parts for the tools, for which it makes a charge. JDI wanted to recover the VAT under the Thirteenth VAT Directive and made a claim. HMRC refused the claim and JDI appealed HMRC's decision to the FTT.

The question the FTT had to consider was whether the VAT charged on the supply of the tools to JDI would have been JDI's input tax had JDI been a taxable person in the UK. The burden of proof lay with JDI, and so it had to show the tools were used for an economic activity.

The FTT considered recent cases concerned with determining when a direct and immediate link could be considered to exist with either the company's particular transactions or business activities in general. To this end the FTT looked at CJEU Sveda (case C-126/14) and Royal Courts of Justice Associated Newspapers Ltd (case [2017] EWCA Civ 54).

The Sveda case focused on a link between the costs of installing a path on Sveda's premises that was free for anyone to use and the supplies Sveda made on those premises, such as sales of gifts and refreshments.

The Associated Newspapers Ltd case focused on a link between retail vouchers Associated Newspapers Ltd bought to give to participants in a business promotion scheme and the company's business activities in general.

In both cases a sufficient link was found to allow the company to recover input VAT.

It was accepted that JDI has an economic activity in selling spare parts for the tools and at the same time no economic activity in leasing the tools for no consideration. The FTT found there was no obvious link between JDI's acquisition of the tools and sale of spare parts. There would need to be a link for the input VAT to be recoverable. Although there is no obvious link, the FTT considered that there is perhaps a link and went on to examine whether this was the case. While it is possible to find an objective link between the acquisition of the tools and the sale of spare parts because JDI is the only source of the spare parts, there is a weakness. This weakness arises from JDI's failure to require that the tools be used frequently, to help increase sales of spare parts, in the lease with Baker Hughes Nederland BV. The link is further weakened by allowing the tools to be used on a call-off basis. There being no charge for the lease, Baker Hughes Nederland BV was under no pressure to use the tools, as there was no need to generate enough income to at least pay the rental charge. The FTT thus concluded that JDI had failed to show that the goods had been used for making taxable supplies.

The ruling

Having examined the economic activity, the FTT found that there was no evidence that JDI was acting as a taxable person when it acquired the tools. Accordingly, the FTT found that JDI had no right to recover the VAT.

In summary, we would point out that under CJEU case law, a taxable person must satisfy two tests to qualify for recovery of input VAT incurred on supplies of goods or services. Firstly, the taxable person must be acting as such at the time of receiving those supplies. Secondly, the taxable person must use the goods or services for making taxable supplies. Both tests are objective in the sense that they must be confirmed by objective evidence and do not depend on the subjective intentions of the taxpayers.

Unemployment benefit after childcare leave

Many new mothers leave their jobs at the end of their childcare leave for a variety of reasons. This article explores the rules governing unemployment benefits awarded immediately after childcare leave and shares our practical experience of how the National Social Insurance (NSI) Agency deals with a new mother that has been employed for some time.

Benefit after childcare leave

Before the NSI legislation was amended, a new mother who left her job for any reason right after her childcare leave was not eligible for a reasonable unemployment benefit because no NSI contributions had been paid for her during her childcare leave. Under the amended legislation the government pays NSI contributions for the new mother during the period she is taking care of her child up to 18 months of age and receiving childcare benefit or parent benefit, in order to provide her with unemployment cover as well.

In general, unemployment benefit is calculated (1) according to the amount of pay subject to NSI contributions in the last 12 months, (2) excluding the last two months before unemployed status was obtained, and (3) excluding the months with the lowest and the highest pay.

In the case of a new mother, however, the unemployment benefit calculation is based on her pay details before she went on her childcare leave.[1] In this case the last two months and the months with the lowest and the highest pay are excluded from the calculation.

Also, if the new mother receives a bonus or any other extra payment during her childcare leave in respect of an earlier period, those payments can also be included as long as they are favourable.[2]

Although this provision of law aims to safeguard new parents against cases where they are left without any means of subsistence, the agency consultants tend to issue diametrically opposed views. In our opinion, this demonstrates a lack of uniform treatment in this area.

For example, if a new mother is employed for a week right after her childcare leave (and receives a small pay), the agency takes the view that this rule no longer applies because she has resumed employment. In that case her unemployment benefit calculation would only be based on that last pay. The agency offices are all agreed on this, but they differ as to how long the new mother is allowed to work right after her childcare leave.

The agency consultants also take the view that this rule does not apply to a new mother who receives a bonus during her childcare leave. In the agency's opinion, such a bonus interrupts the period (when income was received for the last time) and the benefit should be calculated from the date she received the bonus. In other words, if she received a bonus for her prior-period performance, say, in the fifth month of her childcare leave, then contributions for the 12-month period will be counted from the fifth month, leaving the pre-bonus months with a zero pay for NSI purposes.

We can hardly agree with this approach taken by the agency consultants, as it defeats the whole object of the exercise. It is currently known that this approach causes many mothers to terminate their employment voluntarily at the slightest sign of insecurity for fear of losing a reasonable unemployment benefit. Such advice certainly discourages new parents from returning to the labour market and prompts them to immediately switch from one benefit to another.

We hope the agency will reach a consensus and assess the situation on its merits.

Exempt intra-Community supplies: does VIES registration matter?

This article explores the ruling made by the Court of Justice of the European Union (CJEU) in Case C-21/16 (Euro Tyre) on 9 February 2017.

What is VIES?

VIES (VAT Information Exchange System) is a search engine owned by the European Commission that helps retrieve data from the VAT databases of all member states. VIES is used for checking whether a company – business partner – is registered for cross-border transactions in the EU. A search can show that a particular EU VAT registration number either –

1. exists, i.e. it is valid (the system will show relevant EU VAT information); or
2. does not exist, i.e. the number is not valid (not entered on the member state's database for various reasons, e.g. there is no such number, its registration is

[1] Section 8(8) of the Unemployment Insurance Act

[2] Section 8(9) of the Unemployment Insurance Act

pending, or the number is not activated for intra-Community transactions). If a business partner claims that he has a taxable person's registration number, but a VIES search does not confirm that claim, the business partner can ask the tax authority in his member state to issue a certificate of VAT registration. The business partner could also be required to register for cross-border intra-Community transactions because there is no uniform procedure across the EU.

Background

Euro Tyre is a Portuguese branch of Euro Tyre BV, a company incorporated under Netherlands law. It is engaged in the import, export and marketing of tyres of various brands for retailers based in Portugal and Spain. On the Spanish market, it sells in part directly and in part through a distributor, Euro Tyre Distribución de Neumáticos SL.

The dispute in the main proceedings concerns several sales made during the period between 2010 and 2012 to the distributor, who was registered as a taxable person for VAT purposes in Spain at the time of those sales. However, the distributor was not yet subject in Spain to the system of taxation of intra-Community acquisitions nor registered in VIES. It was not until 19 March 2013 that the Spanish tax authority granted intra-Community operator status and entered the distributor on VIES with retroactive effect from 1 July 2012.

Euro Tyre declared those sales to be intra-Community supplies and thus exempt under article 14(a) of the Portuguese VAT rules for intra-Community trade.

Following a VAT audit covering 2010–2012, however, the Portuguese tax authority claimed that the article 14(a) conditions for a VAT exemption were not satisfied because the distributor was neither registered for intra-Community transactions in Spain nor entered on VIES at the time of those sales.

Consequently, the Portuguese tax authority adjusted the VAT due from Euro Tyre for 2010–2012 together with interest for late payment. Euro Tyre challenged those adjustments.

Preliminary questions

1. Must articles 131 and 138(1) of Directive 2006/112/EC be interpreted, in respect of an intra-Community supply of goods, as precluding a member state's tax authority from refusing to grant a VAT exemption to a seller domiciled in that member state on the grounds that the buyer, domiciled in another member state, is neither registered in VIES nor subject in that country to a system of taxation of intra-Community acquisitions, although he holds, at the time of the transactions, a valid VAT number in that other member state, which has been used on the invoices, and the cumulative material conditions for an intra-Community supply are satisfied, namely, the right to dispose of the goods as owner has been transferred to the buyer and the seller has established that these goods were dispatched or transported to another member state and that, after the dispatch or transport, those goods physically left the member state of departure and were delivered to a taxable buyer, or to a legal entity acting as such, in a member state other than that in which the dispatch or transport began?
2. Does the principle of proportionality preclude an interpretation of article 138(1) of the directive to the effect that the benefit of the right to a VAT exemption is to be denied where the seller, domiciled in a member state, was aware that the buyer, domiciled in another member state, although holding a valid VAT number in that other member state, was not registered in VIES nor came under a system of taxation of intra-Community acquisitions, but the seller was convinced that the buyer would be retroactively registered as an intra-Community operator?

The ruling

The CJEU analysed the question whether VIES registration is necessary for exempting intra-Community supplies from VAT.

The CJEU finds that articles 131 and 138(1) of the directive must be interpreted as precluding a member state's tax authority from refusing to exempt an intra-Community supply from VAT on the sole ground that, at the time of that supply, the buyer, who was domiciled in the member state of destination and held a valid VAT number in that member state, is neither registered in VIES nor comes under a system of taxation of intra-Community acquisitions, where there is no sound evidence pointing to the existence of fraud and it is established that the basic conditions for the exemption are satisfied. In that case, article 138(1), interpreted in the light of the principle of proportionality, also precludes such refusal where the seller was aware of the buyer's circumstances relevant to VAT treatment and was convinced that the buyer would later be registered as an intra-Community operator with retroactive effect.

Thus, the CJEU stated that the requirements for the buyer to obtain a VAT number valid for intra-Community transactions and to be entered on VIES are not essential for transactions to be exempted from VAT. These are formal requirements that cannot deny the supplier's right to exempt supplies from VAT if the substantive conditions laid down by the directive for an intra-Community supply are satisfied.

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Poland

Application of the limited tax liability rule to non-residents deriving income form services rendered to Polish tax residents

In short

On 15 May 2017 the Supreme Administrative Court (hereinafter also referred to as "SAC"), in the extended composition of seven judges, issued a judgment determining the criteria of applying the limited tax liability rule to non-residents deriving income form services rendered to Polish tax residents outside of the territory of Poland. Prior to the latest amendment of the CIT Act, this issue aroused many controversies due to the inconsistent court practice.

Detailed information

The provisions of the CIT Act that were in force prior to 1 January 2017, did not provide any guidance on how to interpret the term "income derived in the territory of the Republic of Poland". As a result, it was unclear whether a non-resident, who provided services abroad for a Polish resident, was subject to WHT in Poland.

The tax authorities and some of the courts argued that in such a case the sole fact of paying the remuneration of the non-resident by the Polish tax resident results in the applicability of the limited liability rule to the said non-resident (and as a result in obligation to withhold tax in Poland).

At the same time other courts disputed this approach, arguing that since the place of performance of the service is not the territory of the Republic of Poland, there is no obligation to collect WHT in Poland.

In aforementioned judgment, the SAC supported the first of these positions, arguing that the place of performance of the services by a non-resident to a Polish resident is irrelevant.

It should be noted that the judgment in question is only applicable to payments made for the benefit of non-residents before 1 January 2017 (i.e. under old rules).

That being said, in case of any doubt and questions related to issue at hand our PwC experts are happy to provide you with required assistance.

Multilateral Instrument to Modify Bilateral Tax Treaties has been signed

In brief

On 7 June 2017 the Multilateral Instrument to Modify Bilateral Tax Treaties („MLI") has been signed in Paris. MLI globally implements mechanisms created to prevent international profit shifting to locations where they are subject to reduced taxation or non-taxation. OECD estimates that it will allow to change ca. 1 100 double tax treaties („DTT") at the moment. Currently, in case of Poland, it is assumed that 47 DTTs will be modified.

In detail

Origins of MLI

Origins of Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting's creation result from works initiated by OECD during Base Erosion and Profit Shifting („BEPS") project.

OECD and G20 countries participating in BEPS project decided that aggressive tax planning poses a significant threat for tax incomes, tax independence and integrity of tax systems of the respective countries.

Goal of MLI

MLI contains solutions aimed at creating mechanisms allowing countries to react against actions which lead to reduction of tax base (base erosion) and transfer of income to jurisdictions offering reduced taxation or non-taxation (profit shifting).

MLI was created in order to quickly and swiftly introduce solutions implemented during BEPS project into existing DTTs.

MLI allows to automatically change DTTs concluded by the respective country, thus eliminating the necessity of conducting long-lasting bilateral negotiations between countries.

Structure of MLI

MLI is divided into seven parts:

- Scope and interpretation of terms (art. 1-2)
- Hybrid mismatches (art. 3-5)
- Treaty abuse (art. 6-11)
- Avoidance of permanent establishment status (art. 12-15)
- Improving dispute resolution (art. 16-17)
- Arbitration (art. 18-26)
- Final provisions (art. 27-39)

Due to the need of including different solutions from international tax law functioning in internal tax systems of MLI signatories, provided regulations are highly flexible. Countries are able to either reject, accept or conditionally accept provisions of MLI.

Provisions regarding treaty abuse and provisions related to resolving tax disputes more efficiently are of obligatory nature – they constitute a so-called minimal standard.

MLI from the Polish perspective

Poland declared 78 DTTs for the MLI's purposes.

Among declared DTTs, there are i.a. DTTs with: Austria, Belgium, Canada, Cyprus, Denmark, France, Holland, Ireland, Luxembourg, Malta, Mexico, Norway, Sweden and the United Kingdom.

DTTs with i.a. USA and Germany are currently out of scope of MLI.

Method of tax credit instead of method of tax exemption

At the moment of signing MLI, Poland has declared 77 DTTs in which method of avoiding double taxation used to this point, i.e. tax exemption method may be replaced by tax credit method.

Principal Purpose Test („PPT")

Principal Purpose Test was chosen by Poland in the transition period as a mechanism of eliminating abuse of benefits resulting from DTT. Goal of conducting the PPT is mainly to find out whether receiving benefit resulting from DTT was one of main goals of a particular arrangement or transaction.

Intended goal of Poland is to introduce to DTTs the additional conditions (determined during bilateral negotiations) limiting the possibility of applying tax benefits resulting from DTTs (limitation on benefits clause).

Permanent establishment

In relation to rules regarding avoidance of permanent establishment status (e.g. by using commisionaire structures) established in MLI, Poland made a reservation that these rules will not be applicable to DTTs declared by Poland.

MLI's entry into force

MLI's entry into force will happen after three months from the date when MLI is ratified by a fifth country.

MLI will be applicable in relation to the particular DTT after both parties of the particular DTT will sign MLI, ratify it and finish other procedures required by their internal law.

OECD foresees that the first changes to DTTs may happen in the beginning of 2018.

Amendment to Social Security Act - one account and new identifiers of contribution remitters from 1 January 2018

In brief

On May 18, 2017, the President of Poland signed the Act from 11 May 2017 amending the Social Security Act. The purpose of the amendment is, among others, introduction of individual contribution accounts for social security remitters to which a single payment for all due amounts as required by the Social Security Institution [hereinafter referred to as ZUS] should be made. The new regulations come into force gradually, with the regulations concerning the individual contribution accounts coming into force on January 1, 2018.

Detailed information

In the current legal status, contribution remitters are obliged to transfer contributions to indicated by ZUS bank accounts in separate payments broken down into:

- social insurance (pension, disability, sickness and work accident insurance contribution),
- health insurance,
- The Labor Fund and Guaranteed Employee Benefits Fund,
- the Bridge Pensions Fund.

According to the amended regulations, ZUS will assign to each contribution remitter an individual contribution account number. Payment made into such an account will unambiguously identify the remitter, so the transfers will not need to include any additional identifiers. What is important, the new regulations abolish the so far practice of making several separate transfers. After the new rules enter into force, each remitter will make only one collective transfer to ZUS.

Until 31 December 2017, ZUS is obliged to generate and advise the existing contribution remitters on the assigned numbers of contribution accounts in paper form via the postal service or in electronic form in the case of those remitters who have created their information profile in the ZUS system. Contribution remitters who will not receive a decision on granting the number of contribution account within the above deadline, should make a request to ZUS so that this number can be granted before the deadline of nearest payment in 2018.

In case of new remitters, the individual contributions accounts will be generated and allocated by ZUS as soon as the contribution remitter's account is created.

The new regulations also introduce changes in the rules of crediting payments paid by contribution remitters to their individual contribution accounts - the oldest receivables will be reconciled first according to the maturity date i.e. from the earliest date of receivables. As a rule, the purpose of the above change is reduction of the late-penalty interest accruing in case of indebtedness in the remitter's account and limitation of the late-penalty interest extinguishment.

What does this mean for me?

As a rule, the new regulations allow the contribution remitters to reduce the number of payments to be made to ZUS (from three or four to one) and limit the amount of information provided on a payment documents.

The additional facilitation for the remitters should be the possibility of settling contributions also in EURO in the territory of European Union.

On the other hand, the new regulations increase the possibility of losing the title for voluntary insurance. This is due to the fact that any failure to meet the deadline to pay contributions or payment in lower amounts than due, will result in the arrears in the social security contributions. Thus, each next payment will be credited towards the principal receivable and interest for delay, which in practice may result in the remitter not being able to determine what part of the amount paid relates to social insurance, health insurance, the Labor Fund and Guaranteed Employee Benefits Fund or the Bridge Pensions Fund. The risk of losing the title to voluntary insurance, and consequently the loss of entitlement to benefits, in particular from social insurance in case of sickness and maternity, may in particular affect individuals conducting business activity, partners in partnerships or shareholders in single-person limited liability companies as well as persons cooperating with the above mentioned insured persons.

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Romania

Romania implements country-by-country reporting requirements

In brief

The Romanian Government passed legislation on 9 June 2017 to implement country-by-country (CbC) reporting requirements in Romania, transposing the provisions of Directive (EU) 2016/881 dated 25 May 2016 into the national legislation.

The new CbC reporting provisions follow the OECD Base Erosion and Profit Shifting (BEPS) Project Action 13 initiative.

As such, Romanian ultimate parent entities controlling a Multinational Enterprise (MNE) group with total consolidated group revenue of more than EUR 750 million will have to file CbC reports with the Romanian tax authorities in line with the new regulations. These provisions will also affect other Romanian companies that are part of an MNE group but are not necessarily parent companies.

In detail

The Romanian Government passed on 9 June 2017 Emergency Ordinance no. 42/2017 to align the Romanian Fiscal Procedure Code and local legislation with the provisions of Directive (EU) 2016/881 dated 25 May 2016.

The new legislation is mainly in line with the EU Directive, but some additional clarifications are provided, such as regarding the penalty regime and the specific provisions detailed below.

Filing requirements

According to the new provisions, a Romanian tax-resident entity that:

- is the ultimate parent entity of an MNE group with consolidated revenues of EUR 750 million or more, and
- is required to prepare consolidated financial statements of the group,

has to file a CbC report with the Romanian tax authorities within 12 months of the last day of the MNE group's reporting fiscal year.

CbC reports received by the Romanian tax authorities will be communicated to other interested foreign tax authorities by means of automatic exchange of information within 15 months of the last day of the fiscal year. For an MNE group's first fiscal year, however, commencing on or after 1 January 2016, the CbC report would have to be communicated within 18 months of the last day of the fiscal year.

The Romanian legislation also provides for filing of CbC reporting by a so-called "surrogate parent", i.e. a Romanian tax-resident entity may be appointed by the MNE group to file a CbC report in Romania on its behalf.

In addition, other Romanian resident entities will be required to file a CbC report if one of the criteria below is met:

- The ultimate parent entity of the group does not have the obligation to file a CbC report in its own jurisdiction of tax residence;

- The jurisdiction in which the ultimate parent entity is resident for tax purposes has a current international agreement to which Romania is a party but does not have a qualifying competent authority agreement in effect to which Romania is a party;
- There is a persistent failure in the automatic exchange procedure with the competent authority of the ultimate parent company required to file CbC reporting.

Content of the CbC report

The information to be included in a CbC report is as follows:

- Aggregated information for each jurisdiction in which the MNE group operates regarding total revenues, profit / loss before income tax, number of employees, income tax paid, income tax accrued, stated capital, undistributed profits, tangible assets other than cash and cash equivalents;
- Information regarding all constitutive entities of the MNE group and their jurisdiction with indications of their main business activities.

The template and the content for CbC reports, including the notification template, is to be published by the National Agency for Fiscal Administration Order.

Penalties

Under the law, failure to provide the CbC report, failure to do so in time or providing incomplete / incorrect data would trigger the following penalties:

- For failing to file a CbC report, the penalty ranges from RON 70,000 to RON 100,000;
- For late filing of a CbC report or for incomplete / incorrect data in a CbC report, the penalty ranges from RON 30,000 to RON 50,000.

Languages in which CbC reports will be shared

The new legislation provides that CbC reports could be exchanged by the Romanian tax authorities with other member states in the Romanian language or in any other official language of the European Union.

Notifications

Romanian resident entities part of MNE groups have to notify the Romanian tax authorities if they are the ultimate parent, the surrogate parent or other Romanian resident entity required to file the CbC report. Alternatively, the Romanian resident entity has to notify the Romanian tax authority regarding the identity of the MNE member filing the CbC report and its residency.

According to the new law, this notification is due by the last day of the MNE group's reporting fiscal year, but no later than the deadline for filing a tax return for the respective constituent entity for the preceding fiscal year.

Entry into force

The effective date of the new legislation is 23 June 2017. The legislation will apply to fiscal years beginning on or after 1 January 2016.

The takeaway

The introduction of CbC reporting is an important step in Romanian TP legislation, as it's the first time that Romanian MNE groups have encountered transfer pricing reporting requirements.

In view of these rules, Romanian parent-entities, but also regular members of large MNE groups and PEs, should:

Assess whether Romanian subsidiaries would be subject to the new requirements and how these would impact on their operations and compliance obligations;

Commence preparations for collecting and reviewing the information needed to be filed under the CbC reporting requirements;

Undertake a risk assessment exercise to identify potential red flags and implement a mitigation strategy.

Significant changes regarding double taxation relief

In brief

Romania joined on 7 June the multilateral convention to implement tax treaty related measures to prevent base erosion and profit shifting ("MLI").

The MLI brings a lot of changes that affect double tax treaties provisions. This alert seeks to clarify the future applicability of the MLI.

In detail

What is the MLI's purpose?

The MLI completes some of the double tax treaties with provisions regarding the prevention of the base erosion and profit shifting from the BEPS plan.

These changes can significantly affect how cross-border transactions are taxed.

What did Romania opt for?

Among the measures proposed by the MLI for which Romania opted, we mention:

- Focus on economic substance of transactions by: introducing a rule according to which the benefit of the double tax treaty cannot be granted if obtaining that benefit was one of the principle purposes of an arrangement or transaction.
- An extensive revision of the permanent establishment concept:

  i. new provisions regarding dependent agent (e.g. with direct impact on commissionaire arrangements);

  ii. assessing preparatory / auxiliary activities considering substance of transactions (i.e. we no longer rely on a specific list of activities provided by the double tax treaty);

  iii. in assessing the existence of a permanent establishment, all activities performed by the same company or a closely related enterprise in a contracting state are considered (anti-fragmentation rule);

  iv. new rules regarding the existence of a permanent establishment in the case of construction works.

- Review of tax residence concept for companies: the place of effective management no longer represents the tie-breaker rule on which the tax residence is automatically set. From now on, resolution of residency conflicts will be made by mutual agreement procedure. In practice, this rule can have a dramatic effect for companies by creating double taxation.
- Dispute resolution:

- Expanding the applicability of the mutual agreement procedure (e.g. for setting the tax residence, or in the case of transfer pricing adjustments).
- NB. Romania did not opt for applying the arbitration procedure if no agreement has been reached after two years through a mutual agreement procedure. This aspect can enhance the uncertainty in cases of conflicts regarding the application / treaty interpretation (leading to double taxation).

- Elimination of exemption method: regarding the avoidance of double taxation, only the credit method will be applied, with the exemption method no longer available in Romania's case.
- Dividend taxation: a new condition on the minimum 365-day holding period has been introduced for application of the more favourable provisions regarding dividends.

A list can be found on the OECD website containing the Romania double tax treaties covered by the MLI and the proposed changes (Romania included in this list all its double tax treaties in force).

When does MLI become effective?

- In practice, the MLI will only produce effects if the following conditions are all met:
  - Both countries party to a double tax treaty have signed the MLI;
  - Both countries included the other state in the MLI list of treaties. To date, only 47 countries from the preliminary list of 91 transmitted by Romania have signed the MLI and included the treaty with Romania on their list sent to the OECD, but the list is still open;
  - Both countries have ratified in Parliament the covered tax agreements and MLI amendments.
- The OECD is to centralise the information provided by each country through an online tool, which will most likely be available by the end of this year.

How does it become effective?

1. When reciprocated (i.e. both jurisdictions opt for the same changes), the adopted provisions of the MLI prevail over the text of the double tax treaty.
2. Where there is no reciprocity regarding the amendments ratified by the two states, the MLI does not produce any effect (with some exceptions). Those jurisdictions have the opportunity to engage in bilateral negotiations, however, in order to reach a consensus or to make amendments to the MLI, even after ratification.

[Source: OECD press release issued on 7 June 2017]

The takeaway

The MLI is an instrument that allows coordinated and effective amendment of double tax treaties, thereby eliminating bilateral negotiations. The changes are many and they impact on a wide range of provisions in the double tax treaties. Companies should analyse these changes in detail in order to assess the impact on their transactions and business models.

ANAF invites individuals - real estate developers to declare property sales income by 30 July

In brief

The National Agency for Tax Administration ("ANAF") has issued a press release inviting individuals - real estate developers to declare their income from the sale of real estate assets from their business patrimony by 30 July 2017.

In detail

An ANAF risk analysis identified situations where individuals had declared income tax on real estate property sales, from their personal patrimony, even though they were supposed to pay income tax on real estate property sales, from their business patrimony, according to Fiscal Code provisions.

Thus, through a notice posted on its website, the tax authority invites individuals – real estate developers with income from the sale of real estate to clarify their tax status by 30 July 2017. Otherwise, after that date, taxpayers may be subject to tax inspection.

[Source: Press release issued by the National Agency for Tax Administration]

The takeaway

Real estate developers identified through the ANAF risk analysis will be subject to tax inspections after 30 July 2017.

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Russia

New controversial court practice on the beneficial ownership of income concept

In brief

In recent months, the courts have issued a number of decisions on the abuse of double tax treaties (DTT), some in favour of the tax authorities and others in favour of taxpayers.

In this report, we will examine two court cases on the question of applying the reduced tax rate under the Russia-Cyprus DTT and, in particular, on the question of identifying the beneficial owner of income.

The first case concerns a dividend payment of RUB 300m on which the taxpayer was assessed an additional tax of RUB 30m as well as penalties and fines in the amount of about RUB 5,5m and RUB 750,000 respectively, because a Cypriot company involved in the deal was not deemed a beneficial owner of the income.

In the second case, the court examined the assessment of the 5% reduced rate on dividend income under the Russia-Cyprus DTT, but the dispute was different. The court applied a literal interpretation of the tax treaty's provisions and ruled that compliance with the formal DTT requirements was sufficient grounds for applying the reduced tax rate.

In detail

Decision No. 15АП-17143/2016 of 13 March 2017 issued by the 15th Appellate Arbitrazh Court[3]

The first case involves Sonus Holdings Limited, a Cypriot company that is the sole shareholder of OAO Leningrad Sugar Refinery. The company satisfied all formal requirements confirming that it acts as a tax resident of Cyprus, as well as met the minimum capital contribution required to apply the reduced tax rate in the dividends article of the Russia-Cyprus DTT. However, the court stated that these criteria were insufficient for applying the reduced tax rate, because the Cypriot company was not a beneficial owner of the income.

In this case, the Russian refinery did not actually transfer the dividends to the Cypriot company, but remitted them to the company's Russian branch. The cash was then converted to foreign currency and moved out of Russia to a third-party foreign company resident in an offshore jurisdiction (the Isle of Man) that has no DTT with Russia.

The court dismissed the tax authorities' position that the Russia-Cyprus DTT does not apply in this case, because the income was paid not to the Cypriot company but to its PE, as there were no evidence that the dividends were paid to the branch directly in connection to its Russian business operations. Taking into account that the branch played an intermediary role in transferring the cash, the court therefore excluded the question of PE from the case at hand.

The Russian branch first converted the received cash to a foreign currency and then, based on a directive from the Cypriot company, transferred it in full to the offshore company within several days. The cash was then used to settle loans issued by the offshore company to Sonus Holdings Limited, yet no evidence was provided to confirm that. There was also no evidence confirming that the Cypriot company actually had the right to distribute the dividends.

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[3] http://kad.arbitr.ru/Card/ea49d46a-a90f-4a72-b781-d29bb94fe1dc

Referencing the commentaries on the OECD Model Tax Convention and Resolution No. 53 of the Plenum of the Supreme Arbitrazh Court of Russia of 12 October 2006, which state that qualifying for tax benefits cannot serve as a stand-alone goal for a business and which prohibit the application of tax treaties for obtaining unjustified tax benefits, the court concluded that the Russia-Cyprus DDT had been applied illegally.

Given that the cash (in the form of dividends) was not actually transferred to Sonus Holdings Limited in Cyprus (but to the company's Russian PE and then remitted to an offshore jurisdiction) and that similar cash allocation structures were used with other Russian plants, the court decided that the dividends in question must be subject to the standard tax rate set by Article 284.3.2 of the Russian Tax Code and may not enjoy the benefits set by the Russia-Cyprus DTT (5% tax rate). Fines and penalties were additionally charged.

Resolution of the Chelyabinsk Region Arbitrazh Court of 3 May 2017 on case No. A76-20508/2016[4]

In this case, SV Property Management Limited, a Cypriot company, purchased shares of PAO Chelyabenergosbyt from a third party. The amount paid for the shares of the Russian entity exceeded the threshold required for applying the reduced tax rate under the DTT. As such, the company satisfied the formal requirement within the DTT to have a direct contribution in the Russian entity that is paying out the dividends.

Nevertheless, the tax authorities attempted to assess an additional tax based on the compulsory application of the 10% rate under the DTT and to impose additional penalties.

Just as in the first case, the Cypriot company was in compliance with the requirement to be permanently located in Cyprus, and was deemed in compliance with the criterion for capital contributions. The court referred to the fact that the Russian MinFin had issued repeated clarifications on the definition of "direct investment in the capital" within the Russia-Cyprus DTT. This term, among other things, implies the purchase of shares on the secondary market, as had occurred in this case.

At the same time, the tax authorities presented arguments showing that no direct investment had been made by the foreign company to the Russian entity's capital, as well as facts confirming that the entirety of the Cypriot company's shares were controlled by a Russian individual. They also attempted to prove that the funds contributed to the Russian entity's capital had originated from Russia and that the Cypriot company had received the funds from related parties as a loan. Therefore, the tax authorities filed an inquiry with the Cypriot tax authorities and the latter announced that the funds used to make the investment had been obtained in a loan from the British Virgin Islands and were then similarly transferred to an offshore jurisdiction to settle an interest-bearing loan.

In the decision, the approach taken by the tax authorities, which suggested cancelling the 5% tax rate and imposing tax at 10%, was considered. We believe it is possible to use a different approach to applying tax rates in the case at hand, if the above-mentioned criteria are fulfilled.

The court believed that the arguments put forward by the tax authorities to confirm that the shares had been purchased in order to transfer ownership to an offshore jurisdiction and apply reduced DTT rates could not serve as grounds for the additional tax assessment.

[4] http://kad.arbitr.ru/Card/8ee9bcdb-19d0-480d-9cd3-ab7a743bcd70

Therefore, the court deemed it sufficient to demonstrate compliance with the formal criteria set by the DTT in order to apply the reduced tax rate of 5% on the dividend income.

At the same time, please note that these cases have yet to be reviewed by the appellate court and the position taken by the court may be not final. We will continue to monitor developments in these cases.

The takeaway

As Russia has no statutory framework that could ensure the strict regulation of provisions regarding the concept of beneficial ownership, court practice serves as the key tool that taxpayers can use to obtain information on the criteria for compliance with the respective definitions set by the Russian Tax Code and DTT.

Again, we face a situation when, in certain cases, compliance with formal criteria is deemed as sufficient grounds for applying DTT rules, but in other cases account must be taken of the whole income payment chain and the ultimate beneficiary.

Therefore, we would like to focus your attention once again on the question of paying passive income to foreign recipients using reduced tax rates under DTTs. We are ready to assist you in confirming the actual right to the income and will keep you informed of the most important developments regarding this matter.

Applying the concept of the beneficial ownership: Russian FTS explanations

In brief

In Letter No. CA-4-7/9270 of 17 May 2017, the Russian Federal Tax Service (FTS) explained its approach to interpreting the concept of the beneficial ownership of income in applying Double Tax Treaty (DTT) provisions. The position taken by the FTS is in line with how court practice is currently shaping up.

The FTS's explanations will be binding for lower-level tax administrations. Therefore, taxpayers should get acquainted with the explanations in order to avoid the possibility of unexpected claims.

Here, we will analyse the explanations and answer certain questions that may concern taxpayers.

In detail

(1) Can OECD documents be used as a guideline for interpreting DTT provisions?

The Russian FTS notes that the courts may refer to the official Commentary on the OECD Model Tax Convention on Income and on Capital when making judgements. The commentaries can be applied based on the provisions set in Articles 31-33 of the Vienna Convention on the Law of Treaties of 23 May 1969. This approach is generally accepted by all countries, including those that are not OECD members. Notably, the Russian Ministry of Finance (MinFin) also refers to OECD commentary for guidance on interpreting DTT provisions.

The Russian FTS notes that primary sources (memoranda of understanding, letters, agreements of parties executed in any other form) and secondary sources (e.g., materials of the process of negotiations) may be used when interpreting DTT provisions. The commentaries to the Model Convention constitute a secondary source in this context. They can be used in the absence of a bilateral agreement between countries on a particular issue, or in the absence of clauses that state the express position of a country toward a certain provision.

(2) Does the beneficial ownership concept apply ONLY to interest, dividends and royalties?

The Russian FTS states that the articles on dividends, interest, and royalties in DTTs use the concept of the beneficial ownership. At the same time, the FTS accepts that the concept can be applied to “various types of income paid by foreign entities”. It appears that the tax service intends to apply this approach as a universal tool for combatting the inappropriate use of DTT provisions. The Russian FTS also referred to court decisions confirming this approach (for example, case no. A11-6602/2016,[5] where the concept was applied to the disposal of interest in a Russian company).

(3) What are the criteria for determining whether a party is the beneficial owner of income?

Russian tax law does not contain any specific beneficial owner test. Instead, the general provisions of the Russian Tax Code and DTTs on this matter have been explained by way of MinFin Letters.[6] The Russian FTS has formulated some guidelines that can help determine whether a particular income recipient meets the criteria of the beneficial owner. Companies that receive income must:

- Have an economic presence in their country of residence;
- Have wide authority to dispose of the income;
- Use the income in their business activities;
- Take independent decisions through their officials;
- Show signs of performing business operations (office, hired staff, general business expenses);
- Receive economic benefit from the income;
- Bear individual risks pertaining to assets;
- Have no legal or actual obligations to transfer the income to third parties (specifically parties not entitled to DTT benefits).

Therefore, please note that a risk exists not only when a taxpayer remits income to a non-DTT jurisdiction, but also when it pays the income in the country that enjoys the lesser tax benefits under a respective DTT. Current court practice confirms this fact (see case No. A40-241361/2015[7], where the court resolved to apply the less favourable rate of 10% under the Russia-Italy DTT instead of the zero rate under the Russia-Luxembourg DTT on interest income).

The Russian FTS also states that the tax authorities must provide a comprehensive assessment of a group’s general economic operations. At the same time, when the tax authorities take decisions on DTT abuse, they may use information received from foreign tax agencies, commercial databases, foreign company registers and other publicly available data.

As for income remittances to third parties, the Russian FTS especially stresses that systematic transit payments can qualify as a sign of DTT abuse. In a recent Tax Flash, we analysed one of the court cases confirming this approach (case No. A32-18982/2016).[8] Please note that this case was not included in the FTS’s explanations.

(4) Is it necessary to identify the beneficial owner in order deny the first recipient right to apply tax treaty benefits?

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[5] http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2017-6.html
[6] http://www.pwc.ru/en/tax-consulting-services/fiscal/fiscal-overview-march-4-61.html
http://www.pwc.ru/en /tax-consulting-services/fiscal/fiscal-overview-june-7-64.html
http://www.pwc.ru/en/ tax-consulting-services/fiscal/fiscal-overview-april-3-72.html
[7] http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2016-1
[8] http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2017-21.html

The Russian FTS announced that the tax authorities do not have to identify the beneficial owner of income. The application of benefits can be denied on the grounds that the first recipient is not the beneficial owner of income. In such cases, regular Russian tax rates shall apply.

In fact, the non-recognition of a party as beneficial owner is a separate tool for preventing the abuse of DTTs.

As it follows from the letter, the tax authorities must take account of documents that confirm a party's actual right to the income in the course of a tax audit, if the confirmation had been provided before the ultimate resolution regarding the audit was issued.

The takeaway

The described approaches applied by Russian FTS are generally in line with the court practice trends that we have covered in previous Tax Flashes.[9] We believe that the biggest controversy here is the application of the concept of actual right to income as an all-purpose tool to combat DTT abuse (i.e. the application of the concept to aspects other than interest, dividends and royalties). As we see, the tax authorities are seeking to apply the concept to tax treaties in the broadest possible sense. Therefore, taxpayers must be ready for potential disputes in this regard.

We would like to remind you that taxpayers must confirm beneficial ownership of income in order to apply the reduced tax rate under DTTs, starting from 2017. Therefore, we recommend that taxpayers prepare the required confirmation form in advance and request the necessary information from their contractors. We will be happy to assist you in preparing these forms, as well as in analysing your circumstances, assessing risks and offering solutions.

A global approach to fighting tax abuse: the Convention signed, DTT regulations tightened

In brief

On 7 June 2017, the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (the "Convention"[10]) was signed by 68 countries, while eight more jurisdictions expressed their intention to join in the near future.

We have previously published a Tax Flash Report on the adoption of the text of the Convention.[11]

To begin with, the Convention was developed as part of the OECD's Action Plan on Base Erosion and Profit Shifting ("BEPS Action Plan").[12] The key objective of BEPS Action Plan is to ensure the proper collection of income taxes in jurisdictions where a given business activity is actually taking place, and to prevent artificial profit shifting to tax havens for the purpose of evading taxes.

The Convention is a universal instrument aimed at the legislative application of BEPS principles across a multitude of double taxation treaties ("DTTs"). At the same time, the Convention allows for a certain flexibility on individual DTTs.

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[9] http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2016-53.html
http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2016-64.html
[10] http://www.oecd.org/tax/treaties/multilateral-instrument-for-beps-tax-treaty-measures-the-ad-hoc-group.htm
[11] http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2016-59.html
[12] http://www.oecd.org/ctp/beps-2015-final-reports.htm

Russia was among the first signatories and, what is particularly noteworthy, expressed the intention to apply the Convention to 66 DTTs[13]—the maximum possible number[14]—including new, non-ratified treaties with Belgium and Brazil, thus establishing among the most stringent interpretations of the Convention.

In an explanatory statement,[15] Russia announced that the Convention will not be applied to DTTs with Sweden and Japan, as separate negotiations are underway on signing new treaties that incorporate the Convention's requirements. Thus, we may draw the preliminary conclusion that all subsequent Russian DTTs will contain similar Convention provisions.

The Convention will enter into force in Russia immediately after its ratification, while the relevant DTT provisions will be changed as soon as Russia's partners have completed the internal procedures that are required to adopt the Convention. Thus, changes to individual tax treaties will be introduced gradually, not immediately.

How the Convention works

Recently, national governments have made a number of coordinated attempts to strengthen legislation in the area of international taxation. As an example, we can point to the more expansive interpretation of the notion of beneficial ownership contained in many DTTs and the widespread use of this notion as a universal tool to fight tax evasion.

In this new phase of measures against tax abuse, national tax agencies are taking the fight to the global level. Countries have agreed to use a global but flexible instrument to enforce uniform BEPS requirements universally.

The Convention will amend DTTs with new provisions that considerably restrict tax benefits. From now on, when determining tax procedures, taxpayers will have to factor in not only national de-offshorisation laws and DTT provisions, but also additional legislation that restricts their eligibility for tax benefits.

Thus, when determining tax regimes, several sources of legislation will now need to be considered:

1) national tax law;
2) DTTs;
3) the Convention, to the extent that the approaches of tax treaty partners coincide (i.e. not only Russia's approach, but also the approach of tax treaty partners, as the latter may in certain cases limit the extensive application of the Convention in Russia).[16]

These issues may complicate how tax legislation is perceived. As such, we recommend paying special attention to studying and interpreting the Convention in full.

The Convention stipulates a number of core measures (the minimum standard) that are mandatory for all countries, as well as optional provisions that countries may choose to apply, depending on how stringent they wish to be.

[13] http://www.oecd.org/tax/treaties/beps-mli-position-russia.pdf
[14] Currently, Russia has 82 valid DTTs with other countries. However, the Convention may be applied only to countries that are Convention signatories or working group members
[15] Regulation No. 963-p, "On Signing the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting", http://government.ru/docs/27781/
[16] http://www.oecd.org/tax/treaties/beps-mli-signatories-and-parties.pdf

Russia has expressed its intention to make its DTTs as strict as possible, including provisions that must be changed under the Convention and provisions that depend on foreign partners

The Convention's mandatory provisions constitute the minimum standard on treaty abuse contained in Actions of BEPS Action Plan, including Action 6.[17] The minimum standard will be introduced as an integral part of all amended DTTs, while the inclusion of the optional provisions will be subject to each country's decision. Under these circumstances, Russia has chosen to apply the Convention almost fully.

First, Russia has stated that the Convention will be applied to all eligible treaties. Thus, all countries that have signed the Convention and have current treaties with Russia will face the tightening of DTT rules.

Second, Russia has unexpectedly expressed the intention to adhere to the strictest possible approach and impose the maximum limitations on providing tax benefits.

Below are the most significant new provisions to be introduced to current treaties.

Mandatory provisions

(1) The Convention establishes a general principle for all DTTs: DTTs may not be used for tax evasion purposes. This notion is expressed in a new DTT preamble and a mandatory provision that limits tax benefits, the so-called Principal Purposes Test ("PPT"). Taxpayers may not receive a respective tax benefit if the principal purpose of an arrangement or transaction is precisely to receive such a benefit. To be eligible for beneficial tax rates, taxpayers must prove that the transaction in question had an economically justifiable purpose.

In addition to applying the PPT, it is significant that Russia is also planning to apply the simplified Limitation on Benefits provision (stipulated by the Convention to relieve countries of the need to develop such provisions on their own). This provision significantly alters approaches to defining entities that have an actual right to income.

(1.1) The Limitation on Benefits provision is an additional measure to the PPT; however, it is noteworthy that it is not part of the mandatory provisions. In fact, this provision establishes a specific list of eligibility criteria that entities must meet in order to receive tax benefits under DTTs. The following are eligible for tax benefits: individuals; the government and government entities; companies or other entities whose principal class of shares are regularly traded on one or more recognised stock exchanges; a variety of non-profit organisations; and entities that exclusively administer or provide retirement benefits to individuals, etc.

A resident of a jurisdiction participating in a tax treaty would also be eligible for tax benefits if they are engaged in the active conduct of a business in one jurisdiction and the income derived from the second jurisdiction emanates from, or is incidental to, that business. However, for the purposes of the Simplified Limitation on Benefits provision, the following activities are not considered as "the active conduct of business" and thus DTT benefits do not apply: operating as a holding company; providing overall supervision of or administration to a group of companies; providing group financing (including cash pooling) or making or managing investments.

Foreign governments that are parties to a DTT may decide whether to apply the Limitation on Benefits provision. If a foreign government chooses not to apply this provision, only the PPT shall apply as, apparently, will be the case with Cyprus, Germany, Luxembourg, the Netherlands, the UK, and many other countries. India is one of the

[17] http://www.oecd.org/tax/preventing-the-granting-of-treaty-benefits-in-inappropriate-circumstances-action-6-2015-final-report- 9789264241695-en.htm

countries that might choose to apply the Limitation on Benefits provision, while Canada has announced its intention to include the provision in its bilateral agreement.

(2) Changes to DTT provisions on mutual agreement procedures ("MAPs"). Under the new mandatory provisions:

- A person may present a case to the competent authority of either party to a DTT to initiate a mutual agreement procedure.
- All DTTs will include the provision that cases must be presented within three years of discovering alleged taxation in a manner inconsistent with the provisions of the respective DTT.
- Any agreements will be implemented regardless of the time limits in the domestic law of the parties to the DTT.

It is noteworthy that Russia has chosen not to support MAP arbitration provisions. This means that MAPs will remain the only means of resolving disputes between Russian and foreign tax authorities. Third-party interventions to settle DTT issues will not be permitted.

Optional provisions

Parties to DTTs may choose how extensively they will apply the following optional provisions. They may also include such provisions in their DTTs on a voluntary basis. However, Russia is planning to include them in the list of changes to be made to DTTs.

(3) Limitations on DTT benefits related to specific types of passive income are among the most significant provisions that can affect foreign investors.

(3.1) The article on dividends will be amended with limitations on reduced tax rates on passive income, which must adhere to the following new criteria on asset ownership: the ownership conditions described in a given DTT must be met throughout a 365-day period prior to any dividend payments. However, this limitation is optional and does not invalidate any other limitations set forth in a given DTT.

(3.2) Provisions on capital gains from the alienation of shares or equity of entities that derive their value principally from immovable property: It is intended to introduce a provision in all DTTs that such gains are to be taxed under the rules of the jurisdiction where the immovable property is situated. At the same time, another provision establishes that testing of the share of immovable property in the value of the assets of a company being sold will be conducted for each of the 365 days preceding the transaction.

(4) DTT provisions on permanent establishments

(4.1) Construction site activities and the prohibition to split up contracts: This provision is aimed at preventing the artificial splitting-up of contracts for separate periods in order to avoid constitution of a permanent establishment. However, this provision will not apply to the exploration and mining of mineral resources.

(4.2) Narrowing the definition for activities of a preliminary or auxiliary character: Business activity does not constitute a permanent establishment only if it is specifically listed as an exception in the DTT and is not the business's primary area of activity. This regulation also forbids the splitting of a business process into separate activities that could be interpreted as "activities of a preparatory or auxiliary character" to avoid constitution of a permanent establishment.

(4.3.) Tightening the rules on agency arrangements: Where a person is acting on behalf of an enterprise and, in doing so, regularly enters contracts, or regularly plays the principal role leading to the conclusion of contracts, then that enterprise shall be deemed to have a permanent establishment.

(4.4) Anti-abuse rule for permanent establishments situated in third jurisdictions: This rule stipulates the right of the jurisdiction that is the source of the income to tax the income of a permanent establishment if it is exempt from income tax in the jurisdiction where it has its headquarters and is eligible for reduced tax rates in the jurisdiction where the permanent establishment is situated.

(5) Hybrid mismatches: provisions related to entities or transactions subject to different treatment in different jurisdictions

(5.1) Transparent entities: The article stipulates that the income of an entity shall be subject to mandatory taxation in one of the jurisdictions. A party to a DTT may refuse to provide tax exemptions or dedictions if the entity did not pay such income tax in the other jurisdiction.

(5.2) Provision on dual resident entities: The issue of dual residence of legal entities is to be decided by mutual agreement among the competent authorities. In the absence of such agreement, dual-resident entities will not be entitled to DTT benefits.

(6) Double taxation elimination methods for Russia will remain the same. The netting method will continue to be used after the Convention is ratified.

The final amendment package for each treaty depends on the approach of each DTT partner.

Even the most rigorous approach could be limited by the other party to a DTT. When determining a course of action, it is important to coordinate efforts in line with the other party to the DTT.

The OECD suggests that the Convention must be applied on a mandatory basis to all DTTs to the minimum standard. Each country may choose how extensively to apply the Convention, but must also consider the approaches of other parties of DTTs.

Thus, Russia's position on the Convention might be altered (except for the minimum standard) for any given DTT by the other party. It is likely that certain DTT partners will seek to soften Russia's approach.

Inevitability of change

It is noteworthy that OECD is planning to monitor the introduction of changes to DTTs. The document released by the organisation stipulates that the countries must report on the course of DTT changes implementation, at least where the adoption of the minimum standard is concerned.[18]

According to this document, the process of reviewing changes to tax treaties will start in 2018, assuming that the first changes stipulated by the Convention will not be introduced until next year. The monitoring will be conducted on a yearly basis, including the publication of annual reports on the introduced changes (the first report will be issued in 2019). This work will also include an impact analysis of the changes introduced by the Convention for every DTT.

The monitoring will cover countries that signed the Convention as well as other countries by analysing the degree to which DTTs comply with the minimum standard.

This approach suggests that the legislative authorities of the signatory countries will seek to ratify the Convention as soon as possible. We expect the first changes as early as 2018, including the ratification of the document by Russia.

[18] http://www.oecd.org/tax/treaties/beps-action-6-preventing-the-granting-of-treaty-benefits-in-inappropriate-circumstance-peer-review-documents.pdf и http://www.oecd.org/tax/beps/oecd-releases-peer-review-document-for-assessment-beps-action-6-minimum-standard.htm

The takeaway

While changes to DTTs will be introduced gradually, the tax authorities may already take into account the basic principles set forth in the Convention. Thus, undoubtedly, special attention will be paid to tracking and controlling the abuse of DTT benefits, including the measures stipulated by the Limitation on Benefits provision. Even though the Convention is not yet in effect and the relevant DTT provisions have yet to be amended, it is recommended to give due consideration to the Convention requirements when structuring a business, in order to avoid or at least mitigate any potential claims from the tax authorities.

It is worth paying attention to MAPs as a new regulation that allows companies to receive prompt answers from foreign tax authorities on a mandatory basis, due to the tightening of procedures for handling enquiries from taxpayers. Notwithstanding the non-inclusion of arbitration provisions, we also expect the competent authorities to improve their dispute resolution practices.

We will be happy to provide additional consultations on issues covered in this Flash Report and specific cases, e.g. whether an entity meets the eligibility criteria for DTT tax benefits. We will also gladly advise you on the mutual agreement procedures. If needed, we can help you restructure your business to comply with the new rules.

Advance pricing arrangements on cross-border transactions and other matters regarding transfer pricing: Planned amendments to the Russian Tax Code

In brief

A recently published draft law includes amendments to the Russian Tax Code (the “RTC”) on advance pricing arrangements (the “APA”) and other matters on transfer pricing.[19] The draft law introduces procedures for conclusion of arrangements on cross-border transactions and amends general provisions for making APAs, in particular, covering transactions made within Russia as well.

The public discussion of the draft law will last till 5 July 2017. The new and amended provisions are expected to come into force in January 2018.

In detail

Concluding APAs

The draft law stipulates that pricing arrangement on cross-border transactions will be based on the agreements established between the Russian Federal Tax Service (“Russian FTS”) and foreign competent authority within framework of the mutual agreement procedures provided by double tax treaties (“DTT”). Thus, the above arrangement will be available exclusively for the transactions involving taxpayers from foreign countries with which the Russian Federation has DDTs.

Furthermore, when it comes to concluding APAs, it should be noted that:

1. Following the draft order on the procedures for concluding APAs involving competent authorities of foreign countries the draft law also stipulates that, in order to conclude an APA, a taxpayer must file an application with both the Russian FTS and the relevant foreign competent authority (the latter should be submitted by a foreign counterparty). If a taxpayer’s counterparty failed to submit an application to the foreign competent authority, the taxpayer must further notify the Russian FTS of

[19] http://regulation.gov.ru/projects#npa=62701

the fact once it has filed such an application. The wording of the draft order on concluding APAs[20] implies that the Russian FTS will not begin negotiating with a foreign tax authority until the similar application is not filed with the foreign competent authority.

2. It confirms a six-month period for the Russian FTS to consider a taxpayer's application for an APA (with the possibility of extending up to nine months). At the same time, it stipulates that the period for considering application for an APA with respect to the cross-border transactions with involvement of the foreign competent authority may be no longer than 24 months (with the possibility of extending up to 27 months).
3. It sets a 30-day period for taxpayers to submit to the Russian FTS a revised draft of an APA (if the Russian FTS has ruled that it was necessary).
4. Crucially, the draft law intends to allow the application of transfer pricing methods set by foreign legislation when concluding APAs. However, in this case, the results from their application must be similar to those that would be received under the methods stipulated by the RTC.
5. The draft law stipulates the following grounds for the Russian FTS to reject APAs:
   - Failure to reach an agreement with the foreign competent authority. In this case, a taxpayer will be allowed to reapply to conclude an APA within three months (if the three-month term is met, no state duty shall be charged). However, in this case, a taxpayer will be able to enter into unilateral APA with the Russian FTS.
   - Failure by the taxpayer to submit a revised draft of pricing arrangement within 30 days.
   - Disagreement by the taxpayer with the resolution on an APA and refusal to sign it (including in the failure to appear).

The existing grounds to reject an APA under the RTC will remain in force. They include:

- Failure by the taxpayer to file documents necessary for concluding an APA, as prescribed by the RTC.
- Failure by the taxpayer to pay the state duty or to pay it in full.
- Non-compliance by the taxpayer with the arm's length rule – the key transfer pricing principle.

6. Taxpayers and the tax authorities may initiate a change in an APA according to standard procedures (this provision applies to both cross-border and domestic transactions). If a change is initiated by the Russian FTS, the taxpayer shall submit a draft of the revised APA and documents as prescribed by the RTC, within 30 days.
7. The grounds for the early termination of an APA by the decision of the Russian FTS are supplemented by the case when the taxpayer refuses to accept the changes initiated by the tax authority (including if the taxpayer fails to submit a revised APA to the Russian FTS within 30 days).
8. When it comes to an APA for cross-border transactions, income (profits, revenues) that a related party could have derived (but did not) shall be also recognised for taxation purposes, even if the transaction results in a smaller amount of tax payable

[20] In an earlier report, we covered the development of a draft order for arrangements on cross-border transactions: http://www.pwc.ru/en/tax-consulting-services/legislation/tax-flash-report-2017-15.html

to the Russian budget system or in a greater amount of loss. In the past, this option was possible only when symmetric adjustments were applied.[21]

9. Transactions on which taxpayers have filed an application to the Russian FTS for concluding APA (if the Russian FTS has neither rejected nor approved the conclusion of such APA) shall not be subject to a transfer pricing audit. This provision will apply to both cross-border and domestic transactions.

Other transfer pricing matters

In addition to changes in the procedures for concluding APAs, the draft law stipulates a number of amendments related to other transfer pricing issues. We would like to highlight the most significant changes:

1. The list of grounds for conducting a transfer pricing audit of controlled transactions will be enlarged to include the following: audits can be conducted based on information from a territorial tax authority that the prices in the transactions among related parties and equivalent transactions are potentially not at arm's length.
2. The officers of territorial tax authorities may become involved in transfer pricing audits.
3. Parties will be recognised as related if the ownership interest (direct as well as indirect) of each preceding party in each subsequent entity is over 50%.
4. The draft law provides for extending the list of controlled transactions to the following:
    - Cross-border transactions involving crude oil and refined products, ferrous metals, non-ferrous metals, mineral fertilisers, precious metals and precious stones (it is no longer required that these goods are recognised as commodities traded on global stock exchanges);
    - A party to a transaction applies the 0% corporate income tax (CIT) rate for which agricultural producers or fisheries are eligible, whereas other parties thereto do not apply the 0% CIT rate on such grounds;
    - At least one party to the transaction applies the 0% CIT rate payable to the federal budget and/or reduced rate of CIT payable to a Russian region's budget on the grounds that it is a resident of an advanced special economic zone or of the free port of Vladivostok;
    - At least one party to the transaction applies the 0% CIT rate on the grounds that it conducts educational or medical activities or provides social services for the public.
5. The draft law stipulates that the accrual method shall be used to estimate the amount of income from the transactions for a calendar year, if the person receiving the income on the transaction does not assess income tax in accordance with Article 25 of the RTC.
6. The draft law stipulates that taxpayers have the right not to file transfer pricing documentation on transaction (or a group of controlled transactions) if the income earned within this transaction is below 5% of the total income on all transactions made between its parties for the respective calendar year. However, the amount may not exceed RUB 10 million (or RUB 60 million for controlled domestic transactions.)[22]

[21] Article 105.18 of the RTC.
[22] Article 105.14.2 of the RTC

7. The draft law sets a 30-day period for taxpayers to submit documents when subjected to the transfer pricing audit (the current RTC refers to the procedure established by Article 93.1 of the RTC).

The takeaway

Hopefully, before long, taxpayers will be able to use these new opportunities to concluding APAs involving foreign competent authorities. The upside is that they will be allowed to conclude APAs for cross-border transactions even if the transaction results in a smaller amount of tax payable to the Russian budget system or in a greater amount of loss. We recommend you to analyse whether this matter is relevant to your operations and start making considering potential opportunities in a view of these positive developments in the tax legislation.

The PwC team will be happy to assist you in preparing applications for concluding APAs and other documents for application to tax authorities.

It should be noted that low-value transactions are expected to be exempted from the requirement to prepare transfer pricing documentation. This change will have a positive effect due to the reduction of the administrative burden on business.

We will be happy to provide support to you in addressing any issues within the transfer pricing law, including the amendments that are currently under development.

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Ukraine

Ukraine's Ministry of Finance makes changes to the Transfer Pricing auditing procedure.

On 16 May 2017, a new Order (The Order of the Ministry of Finance #399 from 30.03.2017) on changes to the Transfer Pricing (TP) auditing procedure became effective.

According to the Order, TP auditing for the period of 2013-2014 is to be performed with the specifications defined by Article 39 of the Tax Code of Ukraine that was in effect before 01.01.2015.

PwC comments:

The Order is important and relevant for companies with so-called "controlled transactions" (e.g. transactions with related-group companies).

If you have any questions, please contact us to receive a detailed consultation.

New rules for providing individual tax consultations in Ukraine became effective on 1 April 2017

On 1 April 2017, changes to the Tax Code of Ukraine[23] regarding the procedure for providing and applying individual and general tax consultations became effective.

From that day on, a written request for receiving individual tax consultation (ITC) should contain essential requisites defined by Article 52 of the Tax Code of Ukraine.

Every ITC, provided in written form, should be registered in the Unified Registry of Individual Tax Consultations (URITC). It is available on the Internet at the following address:

https://cabinet.sfs.gov.ua/cabinet/faces/public/reestr.jspx

The Fiscal State Service is in charge of registering ITCs in the URITC[24].

ITC provided to taxpayers starting from 1 April 2017, protects them from possible fines and penalties for the violations of the tax legislation on tax issues that were covered by that ITC. Still, the ITC will not shield from additional tax assessments. Any ITC that is not registered in the URITC will provide no such protection.

The National Bank of Ukraine continues to ease currency control restrictions

On 25 May 2017 the National Bank of Ukraine issued a resolution (The NBU Resolution No. 41 dated 25 May 2017), which further eases certain currency control restrictions, in particular:

Starting from 26 May 2017:

- The settlement period for import-export transactions in foreign currency is now increased to 180 days (previously it was 120 days).

[23] The Law of Ukraine "On changes to the Tax Code of Ukraine regarding improving the investment climate in Ukraine" #1797-VIII dated 21.12.2016.
[24] Respond to the taxpayers' request to obtain an ITC is carried out according to the Procedure approved by the Order of State Fiscal Service #293 dated 25.04.2017.

Starting from 12 June 2017:

- Remittance of funds to foreign investors related to the disposal of shares/corporate rights, charter capital decrease and exit of foreign investors from legal entities is now allowed in the amount not exceeding an equivalent of USD 5 million per month;

- Early repayment of loans secured by international financial organizations (e.g. guarantee, letter of credit, etc.) is now permitted.

Also, the National Bank of Ukraine reinforced the requirement to disclose information on final beneficiary owners of non-resident creditors when registering loan agreements with the central banking authority. The new more stringent requirement will come into effect on 12 June 2017.

We will continue to monitor the developments and keep you updated on the issue.

First Advance Pricing Agreement initiated

The State Fiscal Service of Ukraine received first application from a large taxpayer with intention to launch the Advance Pricing Agreement (further –the "APA") process for the transfer pricing purposes.

A quick reminder: APA procedure is a formal process between a large taxpayer and the tax authorities, which allows business and government to agree on transfer pricing approach to specific transactions for up to 5 calendar years. If the business follows the agreed approach, the government protects this business from tax assessment and penalties in respect of transactions covered by the APA.

This news is a good sign to business to consider the application for APA, if relevant. We are ready to support your business in this regard.

The National Bank of Ukraine continues its policy of currency control liberalization

On 30 May 2017 the National Bank of Ukraine (further – the "NBU") issued a resolution (NBU Resolution No. 44 dated 30 May 2017), which further eases certain currency control restrictions, in particular:

- The ban on purchase of foreign currency by business entities, private entrepreneurs and representative offices in Ukraine having foreign currency in the amount exceeding USD 100,000 (or its equivalent) on their current and/or deposit accounts is now lifted (effective from 31 May 2017);

- The ban on transfers of foreign currency abroad by individuals for non-commercial operations in the amount not exceeding UAH 150,000 is now lifted as well (comes into effect on 12 June 2017).

However, the NBU extended the requirement for mandatory sale of 50% of foreign currency proceeds until 13 December 2017 (NBU Resolution No. 45 dated 30 May 2017).

We will continue to monitor the developments and keep you updated on the issue.

The President of Ukraine signed draft law on "squeeze-out"

On 1 June 2017 the President of Ukraine signed a Law (Law No. 1983-VIII dated 23 March 2017) that introduces important changes to the way Ukrainian joint stock companies operate, in particular:

i. The law introduces a “squeeze-out” and “sell-out” procedure in Ukrainian joint stock companies.

ii. Changes in the type of a joint stock company or its transformation into another type of legal entity no longer require renewal of permits, licenses or introduction of the respective amendments into lease agreements.

The new Law will come into effect on the following day after its publication.

Changes to simplify Ukraine’s legislation on issuance of work permits for expatriate employees introduced

On May 23 the Ukraine's Parliament adopted a draft law (Draft Law of Ukraine “On introduction of changes to certain legislative acts of Ukraine regarding elimination of barriers to foreign investments” №4541 dated 28 April 2016) designed to simplify the procedure for obtaining work permits (WP) as follows:

- The list of documents required for the WPs issuance/extension was significantly shortened.
- It is now possible to obtain a WP under a simplified procedure for founders/shareholders and beneficiaries (controllers) of Ukrainian legal entities.
- The following minimum amount of salary that should be paid to expatriate employees was established: (i) 5 minimum statutory salaries for non-commercial organisations (currently the amount stands at UAH 16,000), and (ii) 10 minimum statutory salaries for all other types of employers (currently - UAH 32,000).
- The term of WPs validity now varies from 6 months to 3 years, as opposed to the previous term of up to 1 year.
- The period of consideration of applications for WP extension is reduced to 3 business days, as opposed to 7 business days previously.
- Employers are required to apply for changes to the issued WP in a number of events within 30 calendar days after such events occur.

The new law is awaiting the President’s signature. It will become effective in three months upon its official publication.

We will continue to monitor the situation and keep you updated on this matter.

The National Bank of Ukraine eases the procedure for investing abroad

On 8 June 2017 the National Bank of Ukraine (further – the “NBU”) issued a resolution (NBU Resolution No. 51 dated 8 June 2017) that changes conditions for investing abroad by Ukrainian legal entities, in particular:

- The amount of permitted investments abroad covered by a single individual license is now increased to the equivalent of USD 2 million per year (previously it was set at USD 50,000 per month);
- Different requirements will apply to obtaining an individual license. These requirements will be based on the amount of the investment, namely:
  - for investments under USD 50,000 per year simplified requirements will apply (shorter list of documents);

- for investments in the amount exceeding USD 50,000 per year -stricter requirements will apply (expanded list of documents, including documents evidencing the economic purpose of the transaction, sources of the funds, information on the ultimate beneficial owners, etc.).

The new rules came into force on 12 June 2017.

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