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Strategic Partners

General Chapter:

1	**The Road to (VAT) Recovery** – William Watson, Slaughter and May		1

Country Question and Answer Chapters:

2	**Albania**	Boga & Associates: Alketa Uruçi & Andi Pacani	7
3	**Andorra**	Arqués Ribert Junyer Advocats: Daniel Arqués i Tomàs & Mireia Ribó i Bregolat	12
4	**Angola**	Manuel Gonçalves Advogados (MGA): Alexandra do Nascimento Gonçalves & Fernanda Mualeia	19
5	**Australia**	Greenwoods & Herbert Smith Freehills: Adrian O'Shannessy & Tony Frost	24
6	**Austria**	Schindler Attorneys: Clemens Philipp Schindler & Martina Gatterer	32
7	**Belarus**	Sysouev Bondar Khrapoutski: Anastasia Malakhova & Andrei Kosov	40
8	**Belgium**	Lexelis Advocaten: Patrick Vanhaute	46
9	**Bolivia**	Guevara & Gutiérrez S.C.: Mauricio Dalman	55
10	**Brazil**	Mattos Filho, Veiga Filho, Marrey Jr e Quiroga Advogados: Luiz Felipe Centeno Ferraz & Renata Correia Cubas	60
11	**Bulgaria**	Baker Tilly Klitou and Partners Business Services EOOD: Svetla Marinova & Radostina Doneva	66
12	**Canada**	Thorsteinssons LLP: Michael Colborne & Michael McLaren	72
13	**Colombia**	Cárdenas & Cárdenas Abogados: Camilo Cortés & Martha Reyes	78
14	**Congo – D.R.**	BTM Lawyers SCA: Natacha Latere & Gustave K. Luzolo	84
15	**Cyprus**	Andreas Neocleous & Co LLC: Elias Neocleous & Philippos Aristotelous	89
16	**France**	Bredin Prat: Yves Rutschmann & Marion Méresse	95
17	**Germany**	P+P Pöllath + Partners: Michael Best & Nico Fischer	102
18	**Ghana**	Bentsi-Enchill, Letsa & Ankomah: Seth Asante & Frank Nimako Akowuah	109
19	**Greece**	Kyriakides Georgopoulos Law Firm: Panagiotis Pothos & Georgia Balopoulou	115
20	**Hong Kong**	DLA Piper: Patrice Marceau & Jennifer Wu	122
21	**Iceland**	LEX Law Offices: Garðar G. Gíslason & Garðar Víðir Gunnarsson	127
22	**Indonesia**	Ali Budiardjo, Nugroho, Reksodiputro: Freddy Karyadi & Chaterine Tanuwijaya	132
23	**Ireland**	Maples and Calder: Andrew Quinn & David Burke	139
24	**Japan**	Nagashima Ohno & Tsunematsu: Shigeki Minami	145
25	**Kazakhstan**	GRATA Law Firm: Assel Ilyassova	152
26	**Kosovo**	Boga & Associates: Alketa Uruçi & Andi Pacani	157
27	**Liechtenstein**	Ospelt & Partner Attorneys at Law Ltd.: Alexander Ospelt & Martin Gassner	162
28	**Lithuania**	Juridicon Law Firm: Laimonas Marcinkevičius & Ingrida Steponavičienė	168
29	**Luxembourg**	MNKS: Raquel Guevara	178
30	**Malta**	Avanzia Taxand Limited: Walter Cutajar & Mary Anne Inguanez	186
31	**Mexico**	Calderón, González y Carvajal, S.C.: Alejandro Calderón Aguilera & Arturo Carvajal Trillo	193
32	**Nigeria**	Bloomfield Law Practice: Bode Adegoke & Busayo Adedeji	199
33	**Norway**	Advokatfirma Ræder DA: Rolf H. Nicolaissen & Sigurd Garmann Tuntland	203
34	**Portugal**	Morais Leitão, Galvão Teles, Soares da Silva & Associados: António Lobo Xavier & António Pedro Braga	209

Continued Overleaf →

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Country Question and Answer Chapters:

35	**Puerto Rico**	Ferraiuoli LLC: Pedro P. Notario-Toll & Reinaldo A. Díaz-Pérez	215
36	**Romania**	Deloitte Tax: Dan Bădin & Daniel Petre	220
37	**Russia**	YUST: Maxim Rovinskiy & Ekaterina Boldinova	225
38	**Senegal**	GENI & KEBE: Rahimine Toure & Ndèye Absatou Ndiaye	231
39	**Sweden**	Kilpatrick Townsend & Stockton Advokat KB: David Björne	236
40	**Switzerland**	Lenz & Staehelin: Pascal Hinny & Jean-Blaise Eckert	244
41	**Ukraine**	ICF Legal Service: Natalya Ulyanova & Oleg Derlyuk	253
42	**United Kingdom**	Slaughter and May: Zoe Andrews & William Watson	259
43	**USA**	Seyfarth Shaw LLP: John P. Napoli & Michael Rosenthal	267

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1 Tax Treaties and Residence

1.1 How many income tax treaties are currently in force in Russia?

There are 80 double tax treaties (agreements) which have been concluded by the Russian Federation and are currently in force. Among them are agreements with China, Cyprus, France, Germany, Italy, Japan, the UK and the USA. The latest agreement was signed with Malta on 24 April 2013.

1.2 Do they generally follow the OECD Model Convention or another model?

In general, double tax treaties follow the OECD Model Tax Convention. However, there are also double tax treaties based on the UN Model Tax Convention, for example with Singapore.

1.3 Do treaties have to be incorporated into domestic law before they take effect?

Pursuant to the Russian legislation, bilateral double tax treaties which change tax legislation in force are to be incorporated by means of ratification.

1.4 Do they generally incorporate anti-treaty shopping rules (or "limitation on benefits" articles)?

Since 2015, there are special anti-treaty shopping rules incorporated in the Tax Code of the Russian Federation (hereinafter "TCRF"). For the purposes of taxation and the application of international tax treaties in the Russian Federation, a person who has an actual right to income shall be a person who, by virtue of direct and/or indirect participation in an organisation or control over an organisation, or by virtue of other circumstances, has the right independently to use and/or dispose of that income; or a person in whose interests another person has the authority to dispose of the income in question.

Where income is paid from sources in the Russian Federation to a foreign person who is a resident of a state/territory with which an international taxation agreement with the Russian Federation exists and who does not have an actual right to that income, if the person who has an actual right to the income in question (or a part thereof) is known to the source of the payment then the income which is paid shall be taxed as follows:

1) Where the person who has an actual right to the income which is paid (or a part thereof) is deemed to be a tax resident of the Russian Federation in accordance with this Code, the income which is paid (or a part thereof) shall be taxed in accordance with the provisions of the appropriate chapters of the TCRF for taxpayers who are tax residents of the Russian Federation, without the relevant tax being withheld at source on the income which is paid (or a part thereof) provided that notice is given to the tax authority with which the organisation which is the source of payment of the income is registered, in accordance with a procedure to be established by the Federal Tax Service of Russia.
2) Where the person who has an actual right to the income which is paid (or a part thereof) is a foreign person who is covered by an international tax treaty with the Russian Federation, the provisions of that international treaty of the Russian Federation shall apply in relation to the person who has an actual right to the income which is paid (or a part thereof) in accordance with the procedure laid down in the international treaty with the Russian Federation.

1.5 Are treaties overridden by any rules of domestic law (whether existing when the treaty takes effect or introduced subsequently)?

Under the Constitution of the Russian Federation part 4 of article 15, "if an international treaty or agreement of the Russian Federation establishes other rules than those envisaged by law, the rules of the international agreement shall be applied". Consequently, if there is a conflict between domestic law and an international tax treaty, the tax treaty prevails.

1.6 What is the test in domestic law for determining corporate residence?

Generally, in Russia the state of tax residence of the company coincides with the state of its incorporation; but also, since 2015, according to the changes to the Tax Code of the Russian Federation (TCRF) a foreign company will be recognised as a Russian tax resident if:

- the place of its effective management is the Russian Federation;
- it can be recognised as a Russian tax resident according to the international tax treaties.

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2 Transaction Taxes

2.1 Are there any documentary taxes in Russia?

Yes, the TCRF contains provisions regulating state duties which are deemed as documentary taxes.

2.2 Do you have Value Added Tax (or a similar tax)? If so, at what rate or rates?

Yes, VAT is applied to the sale of goods, work, services and property rights. There are three rates: 18% (base rate); 10% (reduced rate – mostly applied to food products); and 0% (applied mostly for exported goods, work and services). Besides these rates, there is VAT imposed on goods imported into Russia.

2.3 Is VAT (or any similar tax) charged on all transactions or are there any relevant exclusions?

Generally all transactions connected with sale of goods, work, services and import of goods are VAT-taxable.

However, pursuant to articles 149 and 150 of the TCRF there are non-taxable operations: for instance, the sale of medical goods and some food products; medical services; services involving the carriage of passengers; and property leases to foreign entities (on reciprocity basis). Also specific types of taxpayers are excluded from VAT (articles 145 and 145.1 of the TCRF).

2.4 Is it always fully recoverable by all businesses? If not, what are the relevant restrictions?

VAT is a recoverable tax under domestic law but with restrictions for certain types of businesses applying special tax regimes.

2.5 Are there any other transaction taxes payable by companies?

No, domestic law does not contain any other transaction taxes.

2.6 Are there any other indirect taxes of which we should be aware?

Yes, there are excise and customs duties.

3 Cross-border Payments

3.1 Is any withholding tax imposed on dividends paid by a locally resident company to a non-resident?

Yes, income in the form of dividends paid from resident to non-resident is taxable at a rate of 15%. The tax rate for profit tax may be reduced to 10% and 5% in accordance with certain double tax treaties.

3.2 Would there be any withholding tax on royalties paid by a local company to a non-resident?

Income in the form of royalties is taxed under domestic law by profit tax at a rate of 20%. Reduced tax rates from 0% to 15% may be stipulated in double tax treaties.

3.3 Would there be any withholding tax on interest paid by a local company to a non-resident?

Interest payments are taxed at 20% if the rate is not reduced by special provisions of double tax treaties to 15%, 10%, 5% or 0%.

3.4 Would relief for interest so paid be restricted by reference to "thin capitalisation" rules?

Yes, under domestic law there is a maximum amount of interest that may be recognised as an expense in case of "thin capitalisation". Also, any positive difference between interest charged and maximum interest calculated in accordance with the TCRF shall be equated for taxation purposes with dividends paid to the foreign organisation in relation to which "thin capitalisation" exists. The tax rate for dividends payable to the foreign company is 15%, unless otherwise provided by an international tax treaty.

3.5 If so, is there a "safe harbour" by reference to which tax relief is assured?

In case of "thin capitalisation", no "safe harbour" is granted. Under recent court practice, even double tax treaties directly stipulating so-called unlimited relief are not considered to be in compliance with national rules of "thin capitalisation".

3.6 Would any such rules extend to debt advanced by a third party but guaranteed by a parent company?

Yes, if a debt is advanced by a third party but guaranteed by a parent company, "thin capitalisation" rules are also applicable.

3.7 Are there any other restrictions on tax relief for interest payments by a local company to a non-resident?

There are no other restrictions concerning tax relief for interest payments by a local company to a non-resident.

3.8 Is there any withholding tax on property rental payments made to non-residents?

A tax at a rate of 20% is to be withheld by Russian organisations as a tax agent from property rental payments made to foreign organisations. Normally, however, income tax treaties allow the withholding of Russian tax only from rental payments for immovable property located in the Russian Federation.

3.9 Does Russia have transfer pricing rules?

Yes, transfer pricing rules (section V.1 of the TCRF) are applicable to "controlled" transactions (mainly these include rather big deals between Russian interdependent parties, deals by Russian companies with foreign interdependent parties and with offshore companies) since 1 January 2012. Currently, a unified court practice does not exist and there is a potential risk of tax recalculation under "controlled" transactions by Russian tax authorities if terms and conditions of such transactions substantially differ from market practice.

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4 Tax on Business Operations: General

4.1 What is the headline rate of tax on corporate profits?

The headline rate of tax on corporate profits is 20%: 2% to the federal budget and 18% to the budget of a subject of the Russian Federation. A subject of the RF can reduce its rate for certain groups of taxpayers (not more than to 13.5%). So, the minimum headline rate in any particular region can be 15.5%.

4.2 Is the tax base accounting profit subject to adjustments, or something else?

Under domestic law there is a significant difference between the tax base of tax on corporate profits and an accounting profit. Basically, the tax base is calculated according to the special rules of the TCRF, while the rules of determining accounting profit are stipulated by Russian accounting legislation and standards.

4.3 If the tax base is accounting profit subject to adjustments, what are the main adjustments?

The tax base is not accounting profit subject to adjustments in Russia. As a general rule, the tax base is determined as the difference between revenues and expenses. Thus, some of the revenues are not taxable; all expenses for tax purposes should be proved by documents and should be economically reasonable. Moreover, some of the "unproductive expenses" are directly specified by the TCRF as non-deductible from the tax base. However, one can find examples of accounting adjustments which are used for corporate taxation, i.e. depreciation or determination of market price of shares through the valuation of the company's net assets.

4.4 Are there any tax grouping rules? Do these allow for relief in Russia for losses of overseas subsidiaries?

Since 2012, "a consolidated group of taxpayers" (hereinafter "CGT") was established – a special legal institute which aims to minimise the tax burden. Under the TCRF, on behalf of the CGT the responsible company calculates and pays corporate profits tax and reports to the tax authorities the appropriate tax return. However, the conditions for the creation of a CGT are hardly achievable at first because of requirements for the size of the aggregate business of the participants. There is no tax relief for losses of overseas subsidiaries under Russian tax legislation.

4.5 Do tax losses survive a change of ownership?

Yes. In general, tax losses survive a change of ownership.

4.6 Is tax imposed at a different rate upon distributed, as opposed to retained, profits?

There is the same tax rate (which is 20%) for distributed and retained profits.

4.7 Are companies subject to any significant taxes not covered elsewhere in this chapter – e.g. tax on the occupation of property?

Most companies are subject to VAT, corporate property tax, land tax and transport tax. Other taxes are more or less specific such as excises, minerals (subsoil) extraction tax, biological resources use fee, water tax, etc.

5 Capital Gains

5.1 Is there a special set of rules for taxing capital gains and losses?

There are no special rules regulating taxation of capital gains and losses. These issues are covered by corporate profits tax rules. Such rules are applicable to the profit-making assets of the investor. The TCRF sets forth rules regulating cases when assets are sold at a higher price compared with the acquisition price. Moreover, if these assets earn interest, it would also be considered as a capital gain.

5.2 Is there a participation exemption for capital gains?

There are some participation exemptions for capital gains in Russia. As an example: there is a tax rate of 0% for the income from selling the shares in Russian companies which (shares) the taxpayer held for at least five years and which (shares): 1) during this period have never been listed; or 2) during this period have been referred to the high-technology (innovation) sector of the economy; or 3) at the moment of acquirement were not listed and at the moment of alienation were listed and referred to the high-technology (innovation) sector of the economy. This rule is applicable to shares acquired after 1 January 2011.

Besides this, there is a specific tax relief (tax rate of 0%) for dividends earned by a Russian company from another Russian company or from a foreign company (excluding offshore companies) if the recipient of dividends held a share of a minimum of 50% for at least 365 calendar days.

5.3 Is there any special relief for reinvestment?

Individuals' income tax is not imposed on the income received from joint-stock companies or other organisations by shareholders of such joint-stock companies or stockholders of other organisations as a result of overestimation of the main assets in the form of additional shares (stock, interest) distributed among the shareholders or stockholders of the organisation in proportion to their interest and types of shares, or as difference between the new and the initial nominal value of the shares or their property interest in the charter capital.

When calculating the taxable base for the tax on corporate profits, the taxpayer does not have to count the income in the form of the value of shares additionally received by the shareholder organisation and distributed among the shareholders upon the decision of a general shareholders' meeting, in proportion to the shares owned by them, or the difference between the nominal value of the new shares received in exchange for the initial ones and the nominal value of the shareholder's initial shares when distributing the shares among the shareholders at the increase of the joint-stock company charter capital (without any changes to the shareholder's share of that joint-stock company).

However, it should be noted that in the above-mentioned cases the total amount of the expenses of purchase of the initial and new shares or interest (deducted from the income when calculating the tax if said shares or interest are alienated) does not change.

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5.4 Does Russia impose withholding tax on the proceeds of selling a direct or indirect interest in local assets/ shares?

Russia imposes withholding tax (applicable to non-resident companies) on the proceeds of selling an interest (stocks and shares) in Russian organisations, more than 50% of the assets of which consist of immovable property located within the territory of the Russian Federation, as well as financial instruments derived from such shares, except for stocks recognised as listed on an organised securities market. When determining the tax base of the amount of such revenues, expenses may be deducted.

6 Local Branch or Subsidiary?

6.1 What taxes (e.g. capital duty) would be imposed upon the formation of a subsidiary?

Only a state duty of the sum of 4,000 roubles (approx. 60 USD) would be imposed upon the formation of a legal entity of any kind in Russia. In addition, the registration of the issue of the stocks during the foundation of a joint stock company must be paid with a state duty of the sum of 35,000 roubles (approx. 500 USD).

6.2 What is the difference, if any, between the taxation of a locally formed subsidiary and the branch of a non-resident company?

There are no specific taxes or fees that would be incurred by a locally formed subsidiary in comparison to a branch of a non-resident company with regard to their business in Russia. A subsidiary established under Russian law, being a separate legal entity, is to pay all Russian taxes and fees applicable to its activities in the Russian Federation and abroad. A foreign company that conducts business in Russia through its branch is obliged to pay Russian taxes and fees applicable to its activity in Russia (the permanent establishment concept). There is a state duty in the sum of 120,000 roubles (approx. 2,000 USD) that would be imposed upon the accreditation of a branch of a foreign company in Russia.

6.3 How would the taxable profits of a local branch be determined in its jurisdiction?

Taxable profits would be determined under a general rule: total income minus total expenses of the branch taxed at a 20% base rate or other applicable rate.

6.4 Would such a branch be subject to a branch profits tax (or other tax limited to branches of non-resident companies)?

Under domestic law there is no special branch profits tax. The general rules regulating taxation of organisations are applicable also to branches that are recognised as permanent establishments.

6.5 Would a branch benefit from double tax relief in its jurisdiction?

A branch of a foreign company that is recognised as a permanent establishment of the company in Russia would not benefit from double tax relief in Russia.

6.6 Would any withholding tax or other similar tax be imposed as the result of a remittance of profits by the branch?

Withholding tax would not be imposed. The branch that is recognised as a permanent establishment of the foreign company in Russia should pay all taxes before remittance of profits.

7 Overseas Profits

7.1 Does Russia tax profits earned in overseas branches?

Russia taxes profits earned in overseas branches, but taxes paid by these branches abroad are credited in an amount no greater than the Russian tax on corporate profits to be paid.

7.2 Is tax imposed on the receipt of dividends by a local company from a non-resident company?

Pursuant to the TCRF, income in the form of dividends derived from foreign companies by a Russian company is taxed basically at a 13% tax rate and at a 0% tax rate in particular cases (see question 5.2).

7.3 Does Russia have "controlled foreign company" rules and, if so, when do these apply?

Since 2015 there are "controlled foreign company" ("CFC") rules in Russia. An organisation is a CFC if:

1) it is not a tax resident of Russia; and
2) an organisation and/or individuals who are tax residents of the Russian Federation, are its controlling entities.

A foreign non-legal entity organisation is also deemed a CFC, if tax residents of Russia are its controlling entities.

A controlling entity is:

1) an entity owning a share of over 25% of the organisation;
2) an entity whose share of the organisation (for individuals – jointly with their spouses and underage children) exceeds 10%, if the share of all tax residents of Russia in the organisation is over 50%; or
3) a person exercising control over the organisation in their own interests or in the interests of their spouse and underage children.

Until 1 January 2016, an entity is ruled controlling if the share of the organisation owned by said entity (for individuals – jointly with their spouses and underage children) exceeds 50%.

The income of a CFC is taxed with the controlling entity at the rate of 20% (with an organisation) or 13% (with an individual).

The income of a CFC is not taxed with the controlling entity (resident) if:

- the income amount of the CFC is relatively small (in 2015: below 50 million roubles; in 2016: below 30 million roubles; in 2017: 10 million roubles or less);

or alternatively in one of the cases below:

a) the CFC is a non-commercial organisation;
b) the CFC is established in the countries of the Eurasian Economic Community;
c) the effective tax rate in a country of the CFC is not less than 75% of Russia's average weighted rate (sub-clause 3 of clause 1 and clause 2 of article 25.13-1 of the TCRF) and

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there is a tax treaty between a country of the CFC and the Russian Federation, on the condition that the CFC country is not included in the list of countries which do not exchange tax information with each other. This list is to be established by the Federal Tax Service;

d) the CFC is an active company (its "passive" income does not exceed 20%);

e) the CFC is an active holding company or active sub-holding company (special criteria are established in clauses 5 and 6 of article 25.13-1 of the TCRF); or

f) special types of companies (banks; insurance companies; emitters of marketable bonds; participants of Production-Sharing Contracts in the sphere of the extraction of minerals; operators of the new offshore hydrocarbon fields) if they match special criteria (sub-clauses 5-8 of clause 1 of article 25.13-1 of the TCRF).

8 Taxation of Real Estate

8.1 Are non-residents taxed on the disposal of real estate in Russia?

Non-residents are taxed on the disposal of real estate in Russia, without exemptions.

8.2 Does Russia impose tax on the transfer of an indirect interest in real estate located in Russia and, if so, what constitutes an indirect interest?

As mentioned above in question 5.4, Russia imposes withholding tax on the proceeds of selling an interest (stocks and shares) in Russian organisations, more than 50% of the assets of which consist of immovable property located on the territory of the Russian Federation, as well as financial instruments derived from such shares, except for stocks recognised as listed on an organised securities market.

In addition, revenues from the realisation (including redemption) of investment units of closed-end mutual funds, relating to the categories of rental funds or real estate funds, are taxable by withholding tax.

In both cases, when determining the tax base of the amount of such revenues, expenses may be deducted.

For a Russia-resident company the transfer of indirect interest in real estate located in Russia (meaning a transaction with the stocks and shares of a legal entity which owns real estate) is taxable as a transfer of stocks and shares (see the rules applicable to capital gains).

8.3 Does Russia have a special tax regime for Real Estate Investment Trusts (REITs) or their equivalent?

Russia does not have a special tax regime for Real Estate Investment Trusts. The transfer of real estate to the trust as well as returning it from the trust is not taxable. The revenues from the trust are taxable and expenses are deductible from the tax base. Losses cannot be taken into account if the founder of the trust and the beneficiary are not the same person. In the case of the foundation of a share investment fund of real estate, the revenues from the shares are taxable in a fairly similar way to those from the securities.

9 Anti-avoidance

9.1 Does Russia have a general anti-avoidance or anti-abuse rule?

Russian legislation does not include special documents with provisions concerning general anti-avoidance rules, but in the TCRF there is a section devoted to transfer pricing (section V.1) and an article determining thin capitalisation rules (article 269).

Although the Russian tax system is largely statutory, court practice in the area of tax regulation is of crucial importance. The decisions of the Constitutional Court of the Russian Federation, the Higher Arbitrazh Court of the Russian Federation (which currently does not exist) and the Supreme Court of the Russian Federation have a significant impact on the interpretation and application of tax legislation. For example, it was court practice that introduced the main elements of fidelity and reasonableness in the Russian tax system (the decree of the Plenum of the Higher Arbitrazh Court of the Russian Federation № 53 dated 12 October 2006).

The doctrine of fidelity and reasonableness in tax relations is now going to be incorporated into the TCRF as there is a draft which is very likely to be introduced in the near future.

9.2 Is there a requirement to make special disclosure of avoidance schemes?

A company taking part in controlled transactions (these mainly include rather big deals between Russian interdependent parties and deals of Russian companies with foreign interdependent parties and with offshore companies) is obliged to disclose the appropriate information. During tax audits the Russian tax authorities may request information on any other suspicious transactions.

Also, the tax authorities periodically publish descriptions of schemes which are considered to be tax avoidance schemes.

10 BEPS and Tax Competitions

10.1 Has Russia introduced any legislation in response to the OECD's project targeting Base Erosion and Profit Shifting (BEPS)?

Under the BEPS Action plan, countries should implement a new format of transfer pricing documentation making taxpayers disclose the group structure and all important details of the business which will be available to the tax authorities of the involved countries (so-called master file, local file and country-by-country reporting). Russian officials declare that similar forms will be implemented in Russia, too. The BEPS Action Plan also includes amendments to the transfer pricing rules regarding certain activities, e.g. transactions with intangibles, etc. Russia has not yet taken any steps in this respect and will probably wait for the OECD proposals. Besides this, the courts in some cases sometimes make reference to the principles of the OECD.

10.2 Does Russia maintain any preferential tax regimes such as a patent box?

In Russia there is no "patent box" regime as it is recognised in European countries (like a special tax regime for Intellectual Property

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revenues). However, there are some special tax regimes for small enterprises, such as a simplified tax system, a single tax on imputed income, a patent system of taxation, and a single agricultural tax. Also, there are some tax preferences for organisations which have acquired the status of participant in a project involving the conduct of research and development activities and commercialisation of the results of those activities in accordance with the Federal Law "Concerning the 'Skolkovo' Innovation Centre".

Note

The information and legislation referred to in this chapter are up to date as at 1 September 2015.

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Maxim successfully represents taxpayers in disputes with tax and financial authorities.

He advises clients in respect of a significant number of M&A, on the following issues:

- taxation in the field of real estate investment;
- the network of retail trade;
- the port industry; and
- investment into agro-industrial assets, etc.

Maxim is recommended by European Legal Experts as an expert on issues of tax law.

As an expert, he took part in the development of a number of bills, including the Federal law on the preparation and holding in the Russian Federation of the FIFA World Cup 2018.

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Ekaterina Boldinova is a Senior Associate at the Law Firm "YUST".

Ekaterina specialises in Tax Law, Litigation and Arbitration.

Prior to joining YUST, she was a senior in-house counsel with one of the leading Russian telecommunication companies.

She advises various clients on measures to prevent claims from tax authorities.

She elaborates documentation for transactions in consideration of possible tax risks.

Ekaterina Boldinova successfully represents taxpayers in disputes with tax authorities. She has acted on claims of more than $500 million in arbitration defending companies regarding payment of VAT, profit tax and all other taxes.

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