



RUSSIAN DEOFFSHORISATION BILL REACHES STATE DUMA



“knowledge”

*Facts, information and skills
acquired through experience or
education; the theoretical or
practical understanding of a
subject.*

OXFORD DICTIONARY

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ΓΝΩΣΗ

Russian deoffshorisation bill reaches State Duma. Latest Update on Taxation of Russian 'Controlled Foreign Companies'.

1.0 Introduction

After several months of discussions, debates and disputes among the Russian Government, its Ministries, tax practitioners and the business community, the draft law on deoffshorisation measures (the "Deoffshorisation Law") was finally submitted to the lower house of parliament, the State Duma, on 22 October 2014.

Businesses however are still hard at work trying to smoothen certain provisions of the bill, therefore further changes to the draft may be forthcoming as the law-making process in Russia clearly allows further changes to be introduced to a submitted bill. Nevertheless, the Deoffshorisation Law is planned to be adopted until the end of the year and enter into force as of January 2015.

Our firm is carefully monitoring developments in relation to the Deoffshorisation Law since its impact on the Russian business environment can hardly be overestimated. You may refer to our **Tax Update v.4 i.4 (EN & RU)** and **Tax Update v.4 i.7 (EN & RU)** for further information.

The present tax update is generally aimed at pointing out certain changes in the current draft of the Deoffshorisation Law as compared to previous drafts. A detailed Tax Update on the final version of the bill will be issued once

2.0 Latest Provisions of the Draft Law

Generally, the new version of the draft law provides for the same three main deoffshorisation measures: (a) beneficial owner of income concept, (b) controlled foreign company (CFC) rules and (c) Russian tax residency rules for legal entities. However, specific regulations relating to these measures changed as compared to the late spring draft and even as compared to the 28 August draft.

In terms of the beneficial owner of income concept, the latest draft of the Deoffshorisation Law confirmed the right of the non-Russian beneficial owner of income to apply the relevant double tax treaty benefits even if this beneficial owner is not the actual recipient of income payable by a Russian company. If the beneficial owner is a Russian company, then the respective Russian tax rules shall apply. These provisions were absent in the late spring draft of the Deoffshorisation Law. We believe these changes to be positive.

CFC rules is the most debated and the most complicated deoffshorisation measure. To remind you of the substance of CFC rules, under the Deoffshorisation Law, Russian tax residents shall be subject to Russian domestic tax on certain undistributed profits received by their CFCs, including structures such as funds, trusts etc.

Generally, under the latest draft of the Deoffshorisation Law, Russian tax residents shall be treated as controlling persons with respect to CFCs if their direct or indirect participation in CFC exceeds 25%. However, a 10% threshold applies in situation when a CFC is actually owned by different Russian residents (even non-related) for more than 50%. The above thresholds is said to enter into force in 2017. During the transitional period, a participation threshold of 50% will apply.

Undistributed profit of the CFC shall be subject to tax in Russia if it exceeds RUB 10m per year, although for 2015 the threshold is RUB 50m and RUB 30m for 2016.

The latest draft of the Deoffshorisation Law introduced an exemption for CFC's profits if income of such CFC consists mainly (for 80%) from active income, as opposed to passive income such as dividends, interest, royalties etc.

Russian tax residents shall notify the authorities on their CFCs, including funds, trusts etc. Besides CFCs, Russian tax residents shall also notify the authorities on their participation in non-Russian companies, even if these companies are not CFCs, if such participation exceeds 10%. First notification shall be filed with the tax authorities no later than April 1, 2015.

The Deoffshorisation Law also provides for certain tax efficient mechanisms to liquidate offshore structures owned by Russian businesses if these businesses decide to move away from the offshore structures in order to avoid complying with burdensome CFC rules.

Among other important issues, it should be noted that the tax sanctions for non-compliance with CFC rules shall not apply for 2015 - 2017. The criminal liability for non-payment of CFC related tax shall not apply for the above years only if this tax is finally paid in full.

The latest draft of the Deoffshorisation Law also provides for more detailed treatment on Russian tax residency rules for legal entities as compared to the late spring draft. In this respect many unclear terms used in the draft (such as "the majority of Board of Directors meetings", "carrying activities on a regular basis" and "guiding management") were clarified. Generally, under the latest draft a non-Russian company shall be treated as managed from Russia (and thus treated as a Russian tax resident) if any of the below conditions are met:

- The majority of Board of Directors meetings of the company are held in Russia
- The executive body of the company carries its activities in Russia on a regular basis
- The guiding management of the company is predominately performed in Russia

There is a number of cases (exemptions) provided by the Deoffshorisation Law when, irrespective of meeting any of the above criteria, a non-Russian company may only itself decide whether to be a Russian tax resident.

Finally, on the latest version of the Deoffshorisation Law, the measure relating to the closure of a loophole in Russian thin capitalization rules was removed.

3.0 The need for reviewing current legal structures

Based on the above, in anticipation of the final adoption of the Deoffshorisation Law we again strongly encourage all our clients to review their current legal structures to determine the potential effect that the Deoffshorisation Law may have on such structures.

Our firm would be very happy to assist you with the analysis (from both the Cyprus and Russian tax perspectives) and advise you on potential solutions if certain weaknesses are identified. And, in any case, we will continue to monitor any developments in relation to the Deoffshorisation Law and keep you informed.

Note:

The tax information contained in this publication is accurate as at the date of its publication and it is issued as guidance only. It should not be solely relied upon to structure business transactions without expert advice.

For professional consultation, please contact the Taxation Department of Costas Tsielepis & Co.