Winter 2016/2017

# BUSINESS QUARTERLY

Association of European Businesses Quarterly Magazine

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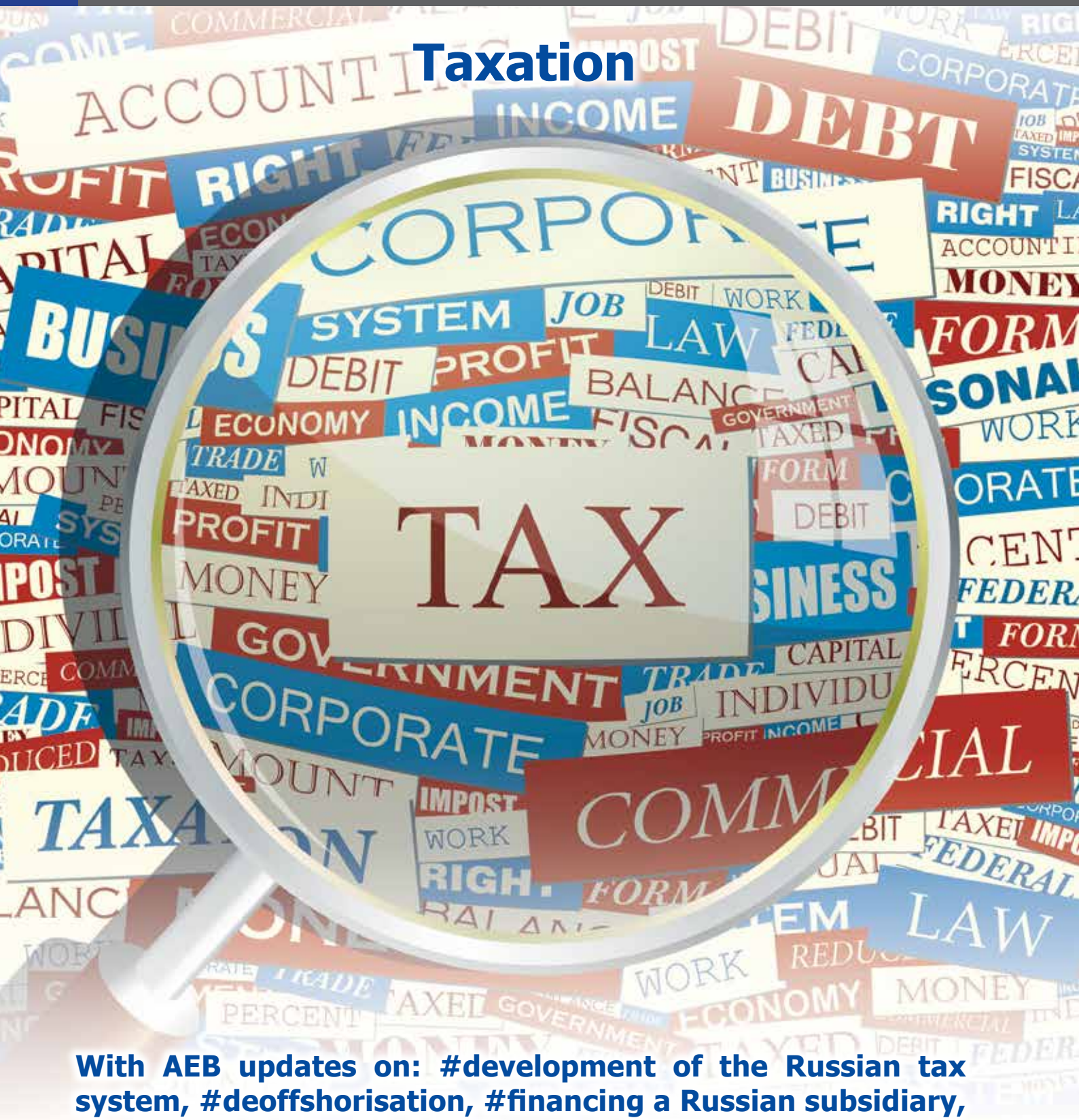


## Taxation

**With AEB updates on: #development of the Russian tax system, #deoffshorisation, #financing a Russian subsidiary, #tax control, #implementation of electronic document flow, #judicial practice in tax disputes, #AEB news, #committee activities, #member news, and #new members.**

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**Dear readers,**

It is my pleasure to introduce the first ever edition of the Business Quarterly magazine dedicated to taxation issues.

The AEB Taxation Committee has a long history – it was established in 1997 – and currently includes more than 200 members from major European companies operating in Russia as well as experts from top consulting, audit and law firms. The committee's work is aimed at monitoring changes to existing legislation and analysing its consequences for business. The following topics were on the radar of the Committee in 2016: excessive taxation on movable corporate property, refusal of VAT recovery due to unfair suppliers, uncertainty in the calculation of VAT for promotional materials and product samples, price control of uncontrolled transactions, invasion in the discretion of entrepreneurs when deducting expenses, and the threat of double collection of a tax debt from companies, to name just a few. I am proud to note that the AEB's voice is often heard by the state authorities and a number of legislative initiatives were amended in accordance with the suggestions presented by the AEB experts.

The magazine will cover the most important taxation issues European companies are facing in Russia such as the beneficial ownership concept, intercompany services, tax benefits, new tax regime for electronic services and many others. As always, the magazine will update you on past AEB events and committee activities.

Enjoy the reading and let me wish every one of you a very Merry Christmas and prosperous 2017!

Sincerely yours,

**Frank Schauff**
Chief Executive Officer,
Association of European Businesses

**Dear readers,**

Welcome to the winter 2016 edition of AEB Business Quarterly, which gives you an in-depth look at the prospects for Russia's tax environment.

In preparing this issue, we have done our best to present you with the most interesting articles and commentary on an issue of major concern to everyone in the Russian business community – is the Russian tax reform at an end?

We all recall President Vladimir Putin's pledge in December 2014 to keep tax rules unchanged until at least 2018. And, so far, lawmakers have lived up to this promise. But will the new, recently elected State Duma continue to pursue the same tax policy?

The short answer is: it is hard to say. The new Duma began its first legislative session by passing a bill that would make multiple amendments to the Tax Code. If enacted, they would consist mainly of clarifications, leaving the core principles of Russia's tax system intact. However, the proposed amendments would not be favourable for taxpayers (e.g. limitations on loss carry forward).

That said, it is undeniable that tax accounting in Russia has become simpler in recent years. And taxpayers can now communicate with the tax office largely online, which is more convenient. In short, life has become easier for Russia's taxpayers. For concrete evidence of this, just look at our country's improved ranking in the World Bank's annual Paying Taxes survey. In Paying Taxes 2017, Russia ranks 45$^{th}$ (up from 47$^{th}$ place in 2016). Meanwhile, our traditional economic partners are lagging behind, with Germany in 48$^{th}$ place, France in 63$^{rd}$, and China in 131$^{st}$. Perhaps this is because Russia's codified tax law puts all tax rules in a single basic document, which any businessperson can easily access.

It is clear that the tax environment is continuously evolving and adapting to changes, while adopting best practices and, when needed, helping to close budget revenue gaps. That is why the AEB Taxation Committee is dedicated to promptly responding to all legislative initiatives, providing business with a public platform to discuss tax issues, and bringing taxpayers' concerns about proposed changes to the attention of lawmakers. We are proud that our voice is heard, our opinion is respected, and the business community sees us as its tireless champion.

On that note, I wish you pleasant reading.

Yours sincerely,

**Alina Lavrentieva**
Chairperson of the AEB Taxation Committee, Partner, PwC Russia

## About the AEB Taxation Committee

As formulated by its membership, the primary mission of the Association of European Businesses (AEB) Taxation Committee is to promote the creation of a favourable tax climate for European companies operating in Russia. Toward this end, the committee is continuously engaged in the systematic development of an entire range of activities.

First of all, committee members constantly monitor the development of Russia's tax system so as to keep the AEB's member companies fully abreast of major changes in tax laws and regulations. The committee's regular meetings provide an open forum for sharing updates on tax matters and collaboratively assessing their potential impact on business, as well as disseminating valuable tax-related information to the AEB community and formulating timely responses to important tax developments.

Each year, the Taxation Committee holds 6–7 working meetings and 3–4 open events, which are of great value to all European and Russian executives who attend. In addition to receiving highly practical tax information, they enjoy a unique opportunity to exchange views with peers and obtain exclusive insights and recommendations from experts. Some open events highlight specific issues, such as transfer pricing or VAT, while others have a special focus on recent changes in tax law, as well as tax administration and enforcement practices. Special focus events are often held in cooperation with other AEB committees, such as the IT and Telecom, Intellectual Property, and Retail Trade committees, among others. Officials from the Russian Ministry of Finance, Ministry of Economic Development and Federal Tax Service, with whom the committee has developed longstanding cooperative relationships, are frequently invited to speak at meetings and events.

As a priority aspect of their overall mission, committee members also formulate the AEB's own position and recommendations on critical tax issues, and actively publicise these views among the greater business community and general public. Based on the outcome of its discussions and meetings, the committee drafts various formal requests, statements, proposals, position papers, and press releases for submission to the relevant Russian Government ministries and federal agencies, the State Duma and the media. This critical activity has repeatedly borne fruit with many of the committee's concerns and suggestions being taken into consideration in the legislative process of drafting new laws and regulations. As well, thanks to the committee's efforts, the fiscal authorities have issued numerous clarifications on various practical tax matters, which benefit not only AEB members but Russia's business community as a whole. In particular, the committee's work has led to the adoption of amendments to the Russian Tax Code and the issuance of official explanations confirming the VAT-exempt status of bonuses paid to customers for meeting commercial objectives under purchase contracts.

In addition to its membership, the committee relies on a 200-strong "brain trust" consisting of tax managers from major European companies operating in Russia as well as experts from top consulting, audit and law firms. Their commitment and experience make it possible not only to pinpoint systemic problems in Russian tax policy and administration, and highlight them to the authorities, but also to propose tailored solutions that conform to best global practice while meeting the country's fiscal needs.

The AEB Taxation Committee represents a unique association of professionals who seek to put their joint knowledge and authority at the service of all businesses and fulfil their social responsibility to the greater community in which they live and work.

**Vadim Zaripov**
Deputy Chairperson of the AEB Taxation Committee, Head of Analytical Department, Pepeliaev Group

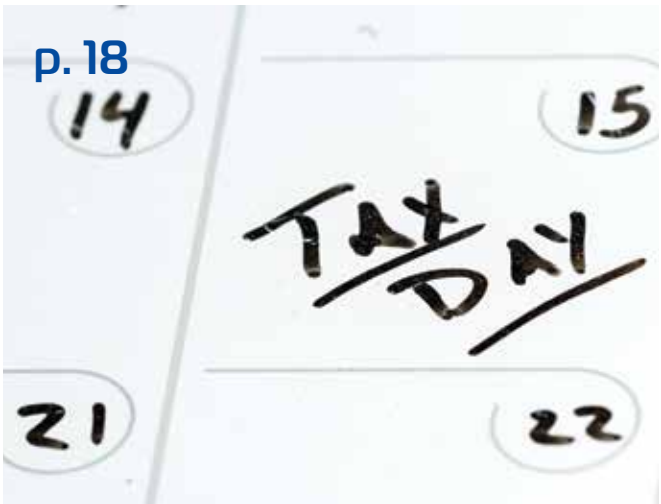
# AEB BUSINESS QUARTERLY, Winter 2016/2017

## Taxation



What is new in the Russian tax system?

What are the changes in the Draft Law on Russian three tier documentation requirements?



Beneficial ownership: take your chance until it is gone.

## AEB Updates



**Sergey Lavrov, Minister of Foreign Affairs of the Russian Federation, meets AEB members**

**AEB holds a briefing by Gabriel Di Bella, Resident Representative of the International Monetary Fund in the Russian Federation**

**AEB organises a briefing by Lev Kuznetsov, Minister of North Caucasus Affairs of the Russian Federation**

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# Development of the Russian tax system: quo vadis?

**ALINA LAVRENTIEVA**
Chairperson of the AEB Taxation Committee, Partner, PwC

Taxes are of major interest to everyone. The way in which the tax system is designed can have a significant impact on economic policy, investment and economic growth.

Russia recently held elections for the State Duma, and the lawmakers just elected or re-elected will soon begin their work as a newly composed legislative body with a fresh mandate. Naturally, all of us are concerned about which specific issues the new Duma deputies will place at the head of their agenda, and particularly whether taxation will remain a top priority. Will Russia's tax law continue to undergo rapid change or can we look forward to greater stability in the tax system?

The answers to these questions depend on a whole host of factors, ranging from the government's ability to top up the federal budget during certain periods to how successfully Russia competes against other countries in terms of creating a favourable business environment, which in turn makes paying taxes easy.

In fact, Paying Taxes is one of the 10 indicators by which the World Bank ranks the 189 economies it tracks in its annual Doing Business rating. In 2016, Russia ranks 47th[1] in terms of Paying Taxes, advancing 17 positions in the past three years. As for our foreign partners, their rankings for Paying Taxes vary from the United States in 53rd place to Germany in 72nd, France in 87th, and China in 132nd place.

Indeed, Russia's success in achieving such a high ranking is well deserved. A critical factor here is that Russian tax law is codified, with all tax rules set forth in a single basic document that is logically structured and that any businessperson can grasp, given enough will and effort.

Some further steps have been taken to make Russian taxpayers' lives easier. The Federal Tax Service of Russia (FTS) has been rolling out more and more new technologies to better serve taxpayers. The times are long gone when accountants had to wait in endless queues at their local tax offices just to file a return. Nearly all interactions with the tax authorities at the reporting and payment stages are now handled online. And, even we average citizens can now visit our personal accounts on the FTS website to review our taxable property, pay taxes, and ask our tax inspectors questions from the comfort of our own homes.[2] In turn, the FTS posts news items of interest to taxpayers on its official website,[3] provides clarifications of the law, and can even assist in verifying the reliability and trustworthiness of business partners. It's all very convenient, isn't it?

Russia has ambitious plans to advance even higher up the World Bank's Doing Business rating. So, taxpayers have ample grounds to look forward to even further streamlining of tax reporting and, at the very least, greater

[1] http://www.doingbusiness.org/rankings

[2] https://lkfl.nalog.ru/lk/

[3] https://www.nalog.ru/rn77/


stability in their tax burdens. No significant increase in the tax burden is expected before 2018 at least, as President Vladimir Putin pledged in his annual state-of-the-nation address to the Russian Federal Assembly in December 2014.[4]

Thus far, Russia's lawmakers have remained "true to their word". Taxes have not been raised in any fundamental way. As recent practice shows, tax collectability is enhanced not by increasing the burden on bona fide taxpayers, but rather by closing various loopholes used in aggressive tax planning schemes. Russian tax law offers various benefits and preferences that may apply if certain criteria are met, making the resulting tax savings perfectly legitimate. That said, just like any other document of such scope, tax law is imperfect and may vary significantly from jurisdiction to jurisdiction. The tax authorities in many countries are actively fighting against practices that abuse and take undue advantage of such imperfections and discrepancies in the law.

The Organisation for Economic Co-operation and Development (OECD) is currently the most authoritative international institution proposing solutions to these problems. Although Russia has not yet acceded to the OECD, we can clearly see that recent key changes in Russian tax law have been aligned with OECD initiatives.[5] For example, with international best practices and OECD initiatives in mind, Russia has recently updated its transfer pricing rules and amended the Tax Code to add controlled foreign corporation (CFC) rules, the concept of beneficial ownership, and the definition of legal entities' tax residency as the place of their effective

[4] http://www.pwc.ru/en/tax-consulting-services/legislation/president-message.jhtml

[5] http://www.oecd.org/tax/

management. These new tools make it possible to collect additional Russian taxes in situations where added value is created in Russia but taxable profits are intentionally transferred to other jurisdictions. What's crucial here is that the new rules will not affect the tax burden on ordinary Russian taxpayers, including small businesses.

To sum up, we are not expecting any major changes in Russian tax law for the foreseeable future. But, this does not mean that we have closed the book on the question of tax reform. Any further changes in tax legislation should, in our view, be especially precise and well-thought-out.

Periodically, we hear calls for raising VAT or for introducing a progressive personal income tax scale, among other proposals. But would such measures really help the government to boost tax revenues? Or, would they merely serve to push businesses back into the shadow economy? What is the precise threshold where it would be fair to levy higher taxes on wealthier citizens? And would the middle class end up feeling the pinch due to such measures more than the high-net-worth individuals for whom they were originally intended? All of these questions call for a thorough analysis and public discussion and we hope that the newly-minted lawmakers will not rush the legislative process.

However, there are certain initiatives that are best not put "on hold." If we seek to prioritise the development of Russia's small and medium-sized enterprise (SME) sector, then we need to continuously work on maintaining a favourable tax environment for SMEs. We can be proud of the fact that, in contrast to many developed countries, Russia offers several special tax regimes for small businesses, including the widely popular simplified tax system. Meanwhile, lawmakers would do well to consider further cutting social security contributions and expanding the pool of eligible small businesses; after all, people are the key asset of any small business and payroll related charges are its heaviest burden.

Turning now to expanding investment in Russia's regions, local authorities should expedite the process of updating regional legislation, especially as they are now authorised under the Tax Code to grant tax preferences for regional investment projects. Under this regime, the corporate income tax (CIT) rate may be reduced significantly, or even brought down to zero for the first few years after the initial returns on an investment are realised.

Investors may also be eligible for certain tax breaks in Special Economic Zones and Advanced Development Zones. In fact, for certain taxpayers, depending on their specific line of business, the property tax and transport tax savings available under such regimes may be even greater than the potential CIT savings. An additional avenue for obtaining tax preferences is the option of concluding a special investment contract with the government, under which the investor pledges to invest at least RUB 750 million.

So, we can say that taxpayers enjoy a truly wide range of options when it comes to choosing where to do business in Russia and which taxes they will need to pay.

Overall, any taxation system is a highly dynamic, continuously evolving structure. Taxes in any given country should closely correspond to the distinctive characteristics and needs of that country, and should be appropriate to its level of economic development. And, moreover, when setting tax policy and determining what is to be taxed and how, lawmakers should never lose sight of the essential need to strike an equitable balance between the interests and needs of the economy, society at large, and the state. On that note, we would like to express our hope that the new State Duma will give proper consideration to the need for such a balance as it takes office and sets to work on drafting new legislation that will determine the future shape and direction of Russia's tax system. Only time will tell…

# Tax incentives for investment activities in Russia: to be or not to be

**NINA GOULIS**
Partner, KPMG

The importance of inbound investment has been growing fast with time: countries competing against countries, and regions competing against regions. The decrease in the tax burden has always been on the top of the list of incentives that governments can grant to make a country or region more attractive.

Russia is hopefully not an exception. However, over the last couple of years, special federal support measures and corresponding tax incentives have primarily been aimed at directing investment towards certain Russian regions (mostly Siberia and the Far East). The list of tax incentives for so-called "Priority Social and Economic Development Areas" (15 regions in Siberia and in the Far East of Russia), and participation in regional investment projects is significant.

The need to extend these investment incentives to other Russian regions, especially given the current economic and political turbulence, has been under discussion and hopefully put into action.

Recently introduced statutory support measures are accompanied by significant tax incentives for investors concluding "Special Investment Contracts" (SPIC).

The SPIC is an agreement between the investor and the Russian Federation, in which the investor takes on the obligation to set up, upgrade or develop industrial facilities in Russia in return for certain state support/incentives and for a stable tax environment. A SPIC can be concluded at the federal and/or regional/municipal level, and therefore the authority held by the governing administrations involved in negotiating a SPIC may differ (either federal, or regional/municipal; or both). A SPIC can be concluded irrespective of the location of the investor in Russia.

The cost of an "entry ticket" for a federal-level SPIC is reasonable for large and medium-sized multinationals at circa EUR 10 million. The "entry ticket" for a regional SPIC may be lower or substituted by other non-monetary criteria. However, the list of incentives in return is impressive:

- profits tax rate: potential reduction to 0%;
- application of accelerated depreciation rates;
- property tax rate: potential reduction to 0%.

The period in which the incentives apply is also impressive – up to 10 years.

All these rates are dependent on the respective regional legislation being enacted, and Russia's regions are actively developing and introducing the respective


legislation to ensure investors can receive these benefits. It is expected that most regions with high investment potential will have enacted the necessary laws by the end of this year, with them taking effect from 2017.

However, the attractiveness of tax incentives should be measured not only by looking at the number of incentives offered, but also by assessing their clarity, ease and consistency of application. At present, there are certain issues related to current tax legislation that may prevent some investors from utilising the full range of incentives stipulated for SPIC participants.

In particular:
• investors are only entitled to reduce the profits tax rate if income from production activities associated with SPIC is not less than 90% of total income. This limitation in most cases prevents existing active companies from enjoying the concessions.
• current legislation places unreasonable demands on how reduced profits tax rates are applied in relation to federal and regional budgets. In particular:
– permission to decrease the regional profits tax rate is provided only to investors that have concluded a federal SPIC. Therefore, investors concluding only a regional SPIC do not enjoy the respective tax rate reductions;
– permission to decrease the federal rate for profits tax is provided for the length of time that regional concessions apply. Therefore, investors concluding a federal SPIC (without involving a region) cannot in fact enjoy the reduced tax rate;
– to qualify for a reduction in the profits tax rate, an investor should operate only in one region (it should not have other production facilities located in other regions).

We have seen increased interest from European businesses with regard to SPICs and how to approach the conclusion of a SPIC (a process that can be quite arduous). Acknowledging the difficulties that may arise when attempting to practically implement the fiscal incentives, the Russian Government is engaged in dialogue with the business community to identify amendments to improve current tax legislation.

What some investors see as equally important for their safe fiscal position in Russia are the declared guarantees of the non-increase of the investor tax burden in Russia for the duration of the SPIC in line with subsidies (for certain industries) and state support measures (e.g. preferential supplier status for state contracts). The respective legislation is still under development.

We hope that these discussions will result in further action to encourage investment incentives "TO BE" rather than "NOT TO BE" in Russia.

*Based on legislation effective as of 20 November 2016.*

# Electronic services subject to fundamentally new taxation regime: measuring the impact on the B2B and B2C markets

**ARSENY SEIDOV**
Partner, Baker & McKenzie

On 3 July 2016, Vladimir Putin, Russian President, signed into law VAT bill No. 244 (the "Law"), which introduces the concept of "services provided through the internet" or electronically supplied services ("ESS" or "e-services") and amends the Russian place-of-supply rules for VAT purposes accordingly effective 1 January 2017. The law completely reshapes the economics for e-services provided by non-resident companies to Russian customers in both the B2B and B2C segments.

## Definition of ESS

The law defines ESS as the provision of services performed through an information and telecommunications network, including the internet, and automatically with the use of information technologies. The definition encompasses a very wide range of services and content provided online (please refer to Article 174.2(1) of the Russian Tax Code for the list of specific ESS).

ESS do not include: (i) the online sales of goods or services that are physically delivered/rendered in Russia; (ii) the sales of licenses for PC software usage rights, computer games and databases on tangible media; (iii) the provision of consulting services by e-mail; and (iv) the provision of internet access services. These categories of operations may be still potentially subject to VAT, including import VAT, under the general tax rules.

Importantly, the law has not abolished the VAT exemption on software use licenses (effective since 2008 and extensively used throughout the country in both purely domestic and cross-border contexts). However, it is expected that this exemption will be revised in the future to match the new policy of VAT taxation of ESS.

## Determining customer location

As of 2017, ESS are deemed provided in Russia for VAT purposes if the customer is considered located in Russia. Specifically, if, with respect to rendering services to an individual, at least one of the following criteria is satisfied, the individual is deemed located in Russia for the purposes of the tax regime:

- the individual's place of residence is in Russia;
- payment for ESS is made through a bank or electronic payment operator located in Russia;
- the customer's network (IP) address is registered in Russia; or
- a telephone number with Russia's country code is used to purchase or pay for services.

Difficulties will likely arise in case of conflict of criteria. However, the law contains a tie-breaker rule basically allowing non-resident suppliers to apply

their discretion to determine the customer location by relying on the laws of another jurisdiction (if such laws also determine the place of rendering of e-services based on the customer location). In order to avoid double VAT taxation, suppliers may need to develop policies resolving such criteria conflicts and agree on their consistent application by their intermediaries who are in fact responsible for collecting and remitting VAT – through respective contractual arrangements and appropriate IT solutions.

For B2B services, the general Russian VAT rules apply to determine whether the customer is a Russian resident or not. If the place of registration of a business customer, as reflected in its corporate documents, is in Russia, then the customer is a Russian resident and services rendered to that customer are deemed to be in Russia for VAT purposes. The law does not provide criteria by which the supplier of e-services may establish that the service is a B2B service.

## Tax registration, payment and reporting requirements

Technically, non-resident companies (whether suppliers or their intermediaries) that collect money from the provision of ESS directly from consumers are required to register for, pay, and report Russian VAT. They must also maintain transaction registers disclosing the cost of e-services to Russian customers and data on meeting the customer residence criteria.

The law does not impose collection and payment obligations on B2B non-resident suppliers. In many instances, "tax agents" of non-resident suppliers, as opposed to the suppliers themselves, are required to calculate and pay VAT on e-services to Russian customers. The law defines the following persons as "tax agents" for the purposes of the tax regime:

- non-resident companies acting as platform companies and other intermediaries that are directly involved in collecting payments from individual Russian consumers;
- Russian companies and individual entrepreneurs acting as intermediaries that are directly involved in collecting payments from Russian customers; and
- Russian companies and individual entrepreneurs that are customers of non-resident suppliers of e-services.

Under this framework, even though the new VAT regime technically applies to both B2C and B2B e-services, the requirement for non-resident companies to pay VAT applies exclusively in the context of B2C services, since VAT in connection with B2B services is collected by Russian intermediaries or corporate customers/individual entrepreneurs.

Importantly, the law refers to non-resident platform companies and Russian companies and individual entrepreneurs as tax agents if they act pursuant to agency, commission or similar agreements with non-resident suppliers. If there are several intermediaries in the supply chain, the lower-tier intermediary that collects money from Russian individuals in most cases is deemed a tax agent even if it does not have direct contractual arrangements with the non-resident supplier.

## PE considerations

Unlike most European jurisdictions, Russia does not have a separate VAT taxpayer registration. If a non-resident company is required to register for tax in Russia for the purposes of the VAT regime, it will be considered registered for general tax purposes. This might potentially give rise to direct tax risks and greater disclosure of taxpayer overseas activities in a Russian tax audit.

Under the express principle of the law, the supply of e-services by a non-resident company to a Russian customer does not give rise to a PE of the non-resident. This rule should, in theory, resolve concerns around the increased direct tax risk for non-resident companies in Russia. At the same time, a non-resident supplier might have some exposure to a Russian PE, especially if it uses a Russia-based server for monetisation and/or processing of customer data. There are ways, however, to legitimately minimise these concerns.

* * *

Overall, the law, especially if coupled with the to-be-revised VAT exemption on software use licenses, will significantly change the principles of taxation of e-services in Russia, their economics and the manner in which non-resident suppliers and marketplaces counteract with foreign and Russian intermediaries and Russian customers. It is obvious that foreign businesses will have to adapt to the new extraterritorial VAT regime and incur associated transition and compliance costs. However, it still remains to be seen how the law will be administered and whether the required tax registration will indeed protect foreign businesses from excessive reporting obligations and corporate profits tax exposure in the long run.

# Draft Law on Russian three tier documentation requirements

**SVETLANA STROYKOVA**
Partner, PwC

**KSENIA LEGOSTAEVA**
Tax Manager, PwC

## Introduction

As a member of the G20, Russia has considered introducing to its tax law certain initiatives from the Base Erosion and Profit Shifting (BEPS) Action Plan developed by the OECD[1]. Already, taking into account the recommendations given in Action 13, the Ministry of Finance has developed a draft law introducing country-by-country reporting (CbCr) requirements (the draft law). Originally the draft law regarding CbCr requirements was released for public discussion[2] on 8 April 2016. There was a significant number of comments provided on the draft law. Therefore, a revised draft law was prepared by the Ministry of Finance, which was revealed to the public on 6 September 2016. The publication was made available on the government website for disclosing draft bills/regulations.

Compared to the April version of the draft law, the revised draft law has been expanded significantly to include:

- The obligation to prepare and submit, in addition to the "country report" (or "country-by-country report"/CbCr in the terminology of OECD), MNC's "global TP documentation" (equivalent of a "master file") and "national TP documentation" (equivalent of a "local file").
- The specifics of the automatic exchange of financial information with foreign countries for tax purposes, as well as the automatic exchange of CbCrs. For this purpose, the entirely new section No. VII-1 is introduced into the Russian tax code.
- A dedicated article aimed at regulating the participation of foreign tax authorities in Russian tax audits.

These changes are proposed to come into effect from 1 January 2017. Introducing the requirement that multinational enterprises (MNEs) prepare and file a CbCr is in line with the OECD recommendations in the final report on Action 13 of the BEPS Action Plan[3].

[1] OECD, Action Plan on Base Erosion and Profit Shifting (OECD 2013), International Organisations' Documentation IBFD. Final reports on the various actions were released by the OECD in October 2015.

[2] The draft law was released on a special government website at http://regulation.gov.ru/projects#npa=41254.

[3] As Russian transfer pricing rules are relatively new (having been introduced in 2012), and the revised draft law anticipates the introduction of the 3 tier documentation requirements to the Russian tax code including the concepts of "Master file" and "Local file".


## Details of Anticipated Legislative Provisions on the CbCr

Under the draft law, MNEs must submit a CbCr. "Multinational corporate enterprise group", which is defined as a group of organisations/members related to each other through ownership and/or control that maintains consolidated financial statements and includes at least one Russian tax resident company and one non-Russian tax resident company (hereinafter the MNE group). Furthermore, the reports must be filed only by the groups with an aggregate revenue of at least RUB 50 billion in the financial year preceding the reporting year as per their consolidated financial statements.

The financial year is defined as the period for which a MNE group's consolidated financial statements are prepared (this period may not coincide with the calendar year). Reports must be submitted within 12 months from the end of the relevant financial year.

Taxpayers that are members of a MNE group must submit notification of their participation in the group to the Russian tax authorities in accordance with the procedures to be established by the Federal Tax Service (hereinafter the tax authorities).

A CbCr must be submitted for financial years starting from 1 January 2017. Under the draft law reports for 2016 may be submitted on a voluntary basis. The following taxpayer members of a MNE group must submit a country-by-country report:

- a parent company of a MNE group (a member that directly or indirectly participates in the capital of other group members);
- a taxpayer that is an authorised member (authorised by the parent company) (referred to as a "surrogate parent" by the OECD); and
- a taxpayer that is a member of a MNE group whose parent company is not required under domestic law to submit a CbCr, or which is a tax resident of a jurisdiction that is not currently party to the international agreement on the automated exchange of information on the

CbCr or a tax resident of a jurisdiction that regularly fails to comply with the requirements for the automated exchange of information.

A taxpayer member of a MNE group may be exempted from filing requirements as regards the CbCr if:
• a CbCr that complies with the Russian tax code must be submitted within 12 months from the end of the respective financial year to the tax authorities of the country where the authorised member of the MNE group is a tax resident (or in which the activities of the member have led to the creation of a permanent establishment); and
• this country requires the filing of a CbCr, is a party to the international agreement on the automated exchange of information on the CbCr and was not notified by the Russian tax authorities about any systematic failures to perform its data sharing obligations.

A CbCr must include the following information:
• total revenue earned from transactions, including from related-party and non-related-party transactions;
• profits (loss) before tax;
• corporate profits tax paid (tax on income (profits) paid by a foreign company);
• corporate profits tax assessed in the current year (tax on income (profits) assessed by a foreign company in the current year);
• shared capital (stated capital);
• accumulated (undistributed) profit;
• number of employees;
• tangible assets other than cash and cash equivalents;
• identification of information about each member of the group, indicating the country of incorporation and tax

residency, as well as the type of activity of each member; and
• other additional information that provides certain details with regards to the above-mentioned information.

Information containing state secrets and/or providing evidence of military and technical cooperation with foreign countries should not be included in the CbCr. The format, completion and electronic submission procedures for CbCrs will be developed by the Russian tax authorities.

The penalty for failing to submit a notification of participation in an MNE group or submission of an inaccurate notification is RUB 50,000, while the penalty for failing to submit a CbCr or submission of inaccurate reporting is RUB 100,000 (for each omission or incorrect item of information). It is intended to relieve taxpayers of the penalties for the above violations identified for 2017–2019.

In addition to the CbCr, Global TP documentation and National TP documentation should be prepared by MNE groups.

Global TP documentation is to be filed by an ultimate parent entity or a surrogate parent entity, if these are Russian entities or Russian tax residents. Otherwise, the draft law does not impose such an obligation on Russian members of an MNE.

Global documentation will have no prescribed form; it should contain the information on MNE group's:
• Structure (including a list of members and description of markets in which the MNE does business).
• Business (including business description; key goods (types of work or services) which contribute more than 5% to the MNE's revenue; key terms of intercompany agreements; a functional analysis of MNE members; information on business restructurings and intangible asset transfers in the financial year in question).
• Intangibles (list of intangibles; description of the MNE's strategy for managing and developing intangibles; description of the transfer pricing policy for R&D transactions, etc.).
• Financial operations (information about the structure of the MNE's financing and transfer pricing policy related to financing transactions).
• Other aspects of business (including consolidated financial statements; information about existing advance pricing agreements and tax rulings concerning intercompany transactions and the allocation of profit among countries).

Overall, the contents of the global documentation is in line with OECD's recommendations set forth in the 2015 final report on Action 13 "Transfer Pricing Documentation and Country-by-Country Reporting".[4]

The deadline for filing the global documentation is three months from receipt of the respective inquiry from the federal tax body, but in any case not earlier than 15 months from the end of the respective financial year.

National TP documentation should be prepared by Russian entities or Russian tax residents (members of MNE groups) in relation to their controlled transactions with foreign entities.

National TP documentation will have no prescribed form; the draft law just establishes what information the national TP documentation should contain, in particular:
• Taxpayer's activity (including management structure, specifics of doing business, competition landscape).
• Controlled transaction (subject matter and key terms; revenues earned or costs incurred; functional analysis of the parties to the transaction; selection of the applicable TP method; calculation of arm's length price or profitability ranges and adjustments made; copies of intercompany agreements, advance pricing agreements and relevant tax rulings, etc.).
• Financial results (financial statements; financial information used for benchmarking analysis; description of information sources, etc.).

The deadline for submitting national documentation is the same as for global documentation.

## Conclusion

A number of comments/amendments have been provided by the business community and accounting firms with respect to the revised draft law. As we understand it, the Ministry of Finance is now analysing suggested changes and comments submitted by the business community during the public hearing on the draft law. Therefore, it was expected that during the autumn session of 2016 the final draft law would be prepared by the Ministry of Finance and submitted for consideration by the Parliament. It is intended that the draft law will pass all required stages of its consideration and be published before the year end to be effective starting from 1 January 2017.

[4] http://www.oecd.org/tax/transfer-pricing-documentation-and-country-by-country-reporting-action-13-2015-final-report-9789264241480-en.htm

# Beneficial ownership: seven reasons to take action before the year end

**VICTOR KALGIN**
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Recent beneficial ownership rules and practice have caught most taxpayers by surprise. Many structures for paying dividends, interest or royalties that have existed for years may not be sustainable any more. The good news is that a lot can be done to meet the challenge. Unfortunately, time is scarce.

For decades, foreign companies that received Russian-source income that was paid abroad and was subject to taxation at source (primarily dividends, interest and royalties) could have enjoyed Russian tax treaty provisions on the basis merely of a tax residency certificate. Taxpayers were used to the established procedure of obtaining certificates from foreign counterparties and enjoyed reduced withholding tax rates. This changed after the "deoffshorisation" campaign that kicked off a couple of years ago when the tax authorities started looking more closely at foreign companies and challenging treaty benefits if those companies appeared to be "intermediaries" or "conduit entities" rather than the ultimate recipients of income (also known as beneficial owners). This campaign has been intensifying and in the future may become one of the main tax challenges for any foreign investor.

Below we list seven reasons why it is so important to think about it before the year end, and explain what can be done to manage the risk.

## 1. Most businesses are affected

There is no doubt that dividends, interest and royalties are sources of income that are relevant to most businesses. In some industries (for example, IT and software) royalties can be one of the major sources of third-party income; in others some of these payment types (or even all of them) occur within the group quite regularly. Companies need to consider whether they can be sure that foreign income recipients can sustain the beneficial ownership test. And yes, both intra-group and unrelated-party transactions should be on the radar.

## 2. The sums in question are usually significant

This follows from the previous point. Not only are dividends, interest and royalties common, their sums can also be very significant. The difference between the alternatives – withholding tax exemption or a 20% rate (which is the case for royalties and interest) – can be quite substantial. This means the issue is worth our utmost attention.

## 3. In many instances it is hard to tell whether there is a problem

The concept itself is ambiguous, making it hard to judge whether in a particular structure reduced withholding tax rates are achievable. One needs to consider multiple factors such as:

- disposal of income;
- functions, risks and assets of the foreign counterparty;
- the company's personnel and management processes;
- the company's tax obligations and business purpose, and so on.

If this level of complexity was not enough, in many instances the required information can be scarce or difficult to obtain. Consider, for example,

third party situations. Can you be sure that in every case your counterparty will provide you with the required details about its business?

## 4. It is an emerging and popular trend in tax audits

Over the last year the number of court cases devoted to the beneficial ownership concept has more than doubled. The following infographics illustrate this and gives other insights into developments in controversy practice:

## 5. Next year there will be a new compliance requirement for documenting the beneficial ownership status

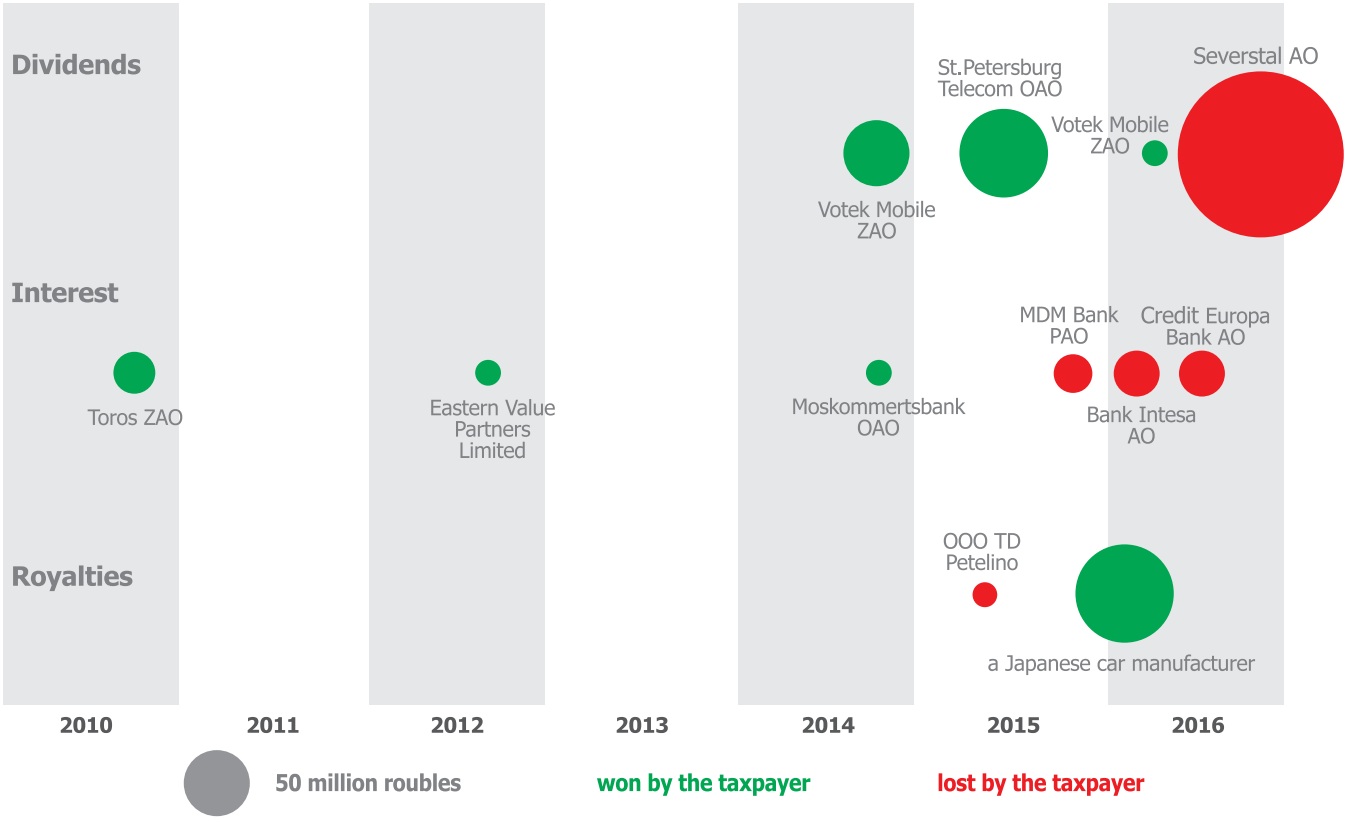
Effective from 1 January 2017, there will be a new requirement to obtain evidence that the foreign company is the beneficial owner of the Russian-source income it receives. This evidence is called "confirmation" in the Tax Code, and the law is silent about its contents or any other details about it, except that it should be in place before the payment of income.

The Russian Ministry of Finance has issued a few clarifications about this document, but they often raise more questions than give answers. Yet it is likely that the tax authorities will treat this document as a prerequisite of the reduced withholding tax rate application, similar to tax residency certificates.

## 6. Some mitigating measures are easy to take

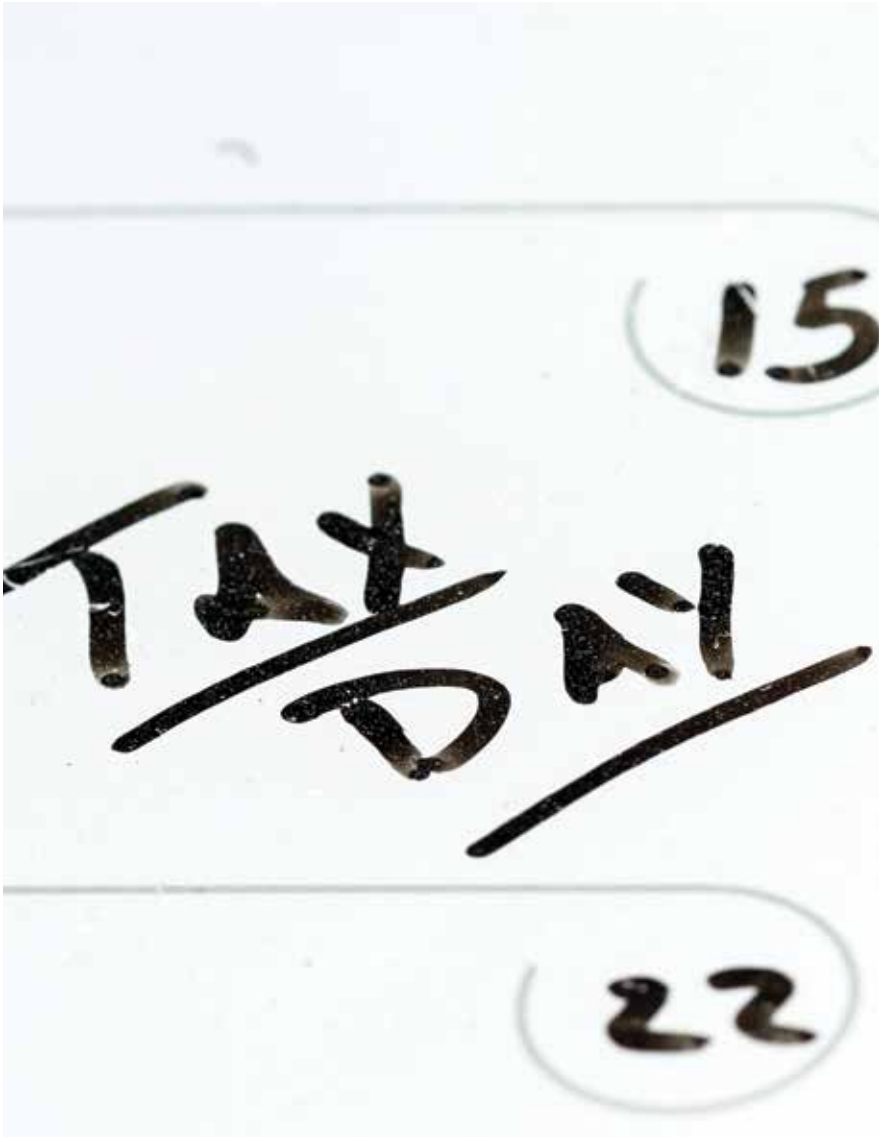
It may not be so costly and difficult to implement some risk-reducing measures, for example:

- Transfer loan receivables, royalty agreements or Russian shares to companies which can better stand the beneficial ownership test (proper substance, multiple functions and diverse assets, etc.).
- Bring different activities associated with finance, license or holding functions into one entity. As a byproduct, this might also help save some compliance and maintenance costs.
- Restructure "back-to-back" arrangements so that there are no obligations in place mirroring the Russian-source




This diagram does not represent all cases where a conduit nature of foreign companies was the reason for tax claims, but rather focuses on those cases where withholding tax was imposed based on the beneficial ownership concept.

This of course is only the tip of the iceberg, since far from all tax audit results are challenged in court.




income (at the very least, the contracts do not have mirroring or connected provisions, such as a sole recourse clause).

• Manage cash flows in a way that income received by the foreign company is not immediately paid to another company. The greater the difference in timing and amounts, as well as the nature of the income, the better.

Any of these measures may not work in third-party transactions, of course, but then the risk becomes a business matter that needs to be discussed and, potentially, the way to manage it is agreed upon with the counterparty. These measures do not fully protect against the risk, but they can be taken relatively quickly. More work might be needed, especially if the sums involved are substantial.

## 7. Other measures can be onerous, but nevertheless should not be delayed

More complex measures include aligning the "form" (legal entities, contracts, etc.) with the "substance" (actual functions, people, etc.), for example:

• relocating people to the countries where key financing, holding and licensing companies are located;

• shifting some operating (trading, production) activities to companies that generate passive income;

• ensuring that companies have sufficient resources to perform their functions and do not need to rely on people and assets located in other countries.

These changes are likely to be expensive and take time, but sooner or later they might become unavoidable in the changing Russian and global tax landscape.

## Three steps to address the problem

The problem is complex and the details are far from clear. However, solving the problem involves three simple steps.

**Step 1.** Identify and quantify the problem. One needs to review cross-border payments out of Russia, identify those subject to withholding tax where reduced rates are applied and assess the risk amount and level.

**Step 2.** If the risk is not tolerable – take restructuring measures. Of course, this is easier said than done. Nevertheless, risks should be addressed on a case-by-case basis (and separately for each potentially exposed transaction) with an emphasis on the most material ones.

**Step 3.** Prepare confirmations and a defence file. A good structure is not good enough without proper documentary support. Apart from confirmations from foreign income recipients, further support may be useful, such as financial statements, contracts, etc.

# Russian deoffshorisation law – impact on foreign investors

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In 2015, Russia introduced several amendments to its tax rules aimed at preventing profit shifting of Russian profits to preferential tax jurisdictions and at re-routing funds back to Russia (deoffshorisation law). The Russian deoffshorisation law, and more specifically the introduction of Controlled Foreign Companies (CFC) rules, requires Russian tax residents to disclose any relevant information on their foreign holding structures, meaning both foreign companies and non-corporate structures. Typically, foreign holding structures were and are still used by Russian beneficiaries for confidentiality reasons and to reduce (or even to evade) Russian taxes. A typical holding structure controlled by Russian beneficiaries would include Russian-based operating companies held by a Cypriot, Dutch or other foreign holding company which, in turn, is held by one or a chain of companies (usually incorporated in low tax jurisdictions). Such companies are usually treated as CFC for their beneficiaries. The new disclosure obligations with respect to such structures effectively eliminate the tax effects of their use, as the profits of Russian CFC are now to be taxed in Russia. Nevertheless, we cannot say that this has led to the mass liquidation of foreign structures. Many Russian businesses are still using the existing structures, and in many cases do not disclose information about them in accordance with the new rules.

What does this mean for foreign investors that plan to acquire an interest in Russian businesses?

First of all, the deoffshorisation law did not make the use of foreign holding structures illegal for Russian residents. As far as legally possible, foreign investors can acquire shares in foreign holdings controlled by their Russian partners. If a Russian group already has a foreign investor, for example an investment fund as a minority shareholder, the participation of this fund is often structured through a joint venture holding company in a foreign jurisdiction. When the investment fund exits from the Russian group, its shareholding in the joint venture company is usually offered for sale.

Furthermore, an investment in a Russian group, if it is structured through a chain of foreign holdings, including those incorporated in a low-tax jurisdiction, does not necessarily entail negative consequences such as an increase in the tax burden for the foreign investor. A German investor, for example, would need to disclose the entire corporate structure, including all intermediate companies, to comply with the reporting obligations in Germany. The overall tax burden, however, would not be higher than a direct investment in a Russian group, at least as long as the German investor holds no more than 50% of the shares (or voting rights) in the Russian group. If the acquired interest exceeds 50%, the offshore structure becomes unprofitable for the German investor (again compared with a direct investment) due to the German national regulation applicable to interest participation in foreign passive companies. There is similar regulation in other European jurisdictions. Consequently, investors may force the Russian groups to restructure their offshore holdings, either at the time when


the interest in the group is acquired by the investor or later.

Another aspect to keep in mind when deciding on the investment and its terms is violations of the deoffshorisation law – by both the company and its shareholders – that may negatively affect the investor.

Where the foreign holding companies of the Russian group are managed and controlled from Russia, for example, by Russian-based management and/or beneficiaries, such foreign companies can be treated as Russian corporate tax residents. The consequence of this is that payments to the foreign companies (for example, interest income, and license or service fees) cannot be exempted from Russian withholding tax through the application of double tax treaties, which would, in turn, lead to additional tax exposure for the Russian group and, indirectly, for the investor.

On the other hand, according to Russian CFC rules tax residents must generally notify the Russian tax authorities of any existing direct or indirect participation in foreign entities and, in some cases, the tax authorities will charge Russian tax on the CFC profits. If the notifications are not filed and/or profits are not taxed in accordance with the rules, these violations do not necessarily constitute an obstacle to the investment. Liability (in the form of financial fines) for the violation of CFC rules is imposed on the company's shareholder, not on the company itself, meaning that there should not be any significant impact on the company's financial results or on the foreign investor.

Based on the above, investors should be advised to diligently assess the level of risk associated with the acquisition of an interest in Russian companies through existing offshore structures. However, potential violations of the deoffshorisation law by their Russian partners should not constitute significant obstacles to investing in Russian businesses.

# The calculation of a tax benefit or price control?

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Disputes over whether a taxpayer has obtained an unjustified tax benefit are of central importance in case law. Recently, an increasingly pressing problem has been the calculation of an unjustified tax benefit a taxpayer has obtained when the tax authority does not contest the fact that the transactions were genuine. Are there any statutory instruments to determine the amount of an unjustified tax benefit in such a situation and whether regional tax authorities are entitled to exercise price control over transactions?

On 20 July 2016, the Panel of Judges for Economic Disputes of the Russian Supreme Court (the "Panel") considered a dispute between Minaevsky Business Centre LLC and Inter-District Inspectorate No. 47 of the Federal Tax Service[1].

Leaving aside the issue of whether the conclusions of the panel are legitimate, we will examine the legal reasoning the panel put forward in its ruling with regard to two issues:

- whether the local tax inspectorate exercised price control for transactions that fall outside the category of controlled transactions;
- whether the Russian Tax Code does not in effect restrict the tax authorities in selecting the technique (method) to determine the price of a transaction for tax purposes when they identify signs of an unjustified tax benefit.

## Did the tax authorities exercise price control?

The ruling points out that the local tax authority did not exercise any price control. The panel once again confirmed[2] that, by virtue of the law[3], it is only the Russian Federal Tax Service that may exercise control over transactions between related parties when the prices they applied deviate from the market level (transfer pricing control), provided that such a transaction is recognised as a controlled transaction.

Recognising it lawful for the local tax authority to have revised the taxpayer's tax obligations, the panel cited signs which the tax inspectorate had established of an unjustified tax benefit being obtained. This was because the price of the buildings which the parties indicated in sale and purchase contracts differed several fold from the market price and the cadastral value.

The key issue lay in how the local tax authorities should determine the amount of an unjustified tax benefit they have detected, which was obtained due to an intentional misrepresentation of the transaction price.

In the opinion of the highest court, to determine the amount of a tax benefit that has been obtained, a tax authority and a court should remodel the tax-

[1] Ruling No. 305-KG16-4920 dated 22 July 2016.

[2] Ruling No. 308-KG15-16651 dated 11 April 2016 (Stavgazoborudovanie LLC).

[3] Articles 105.3(2), 105.5(1), 105.6, 105.7(1) and 105.17 of the Tax Code and article 4(5) of Federal Law No. 227-FL dated 18 July 2011.

payer's transactions in accordance with their actual economic rationale and should determine the scope of rights and obligations based on the genuine economic content of the transaction. In other words, no price control is taking place, but rather the amount is being determined of a tax benefit that has been obtained.

We could have agreed with this approach if it were not for the reasoning of the panel regarding the substantial deviation of the prices the taxpayer applied from market prices[4]. The panel pointed out that tax arrears were determined in a lawful manner, "based on the amount of tax which would have been paid if the property was sold by similar taxpayers undertaking transactions with non-related parties".

If we look at the definition of market price, which is given in article 105.3(1) of the Tax Code, it is clear that the panel, without expressly stating so, refers to the determination of tax arrears based on the market price of the corresponding transaction. The tax inspectorate did not make any claims regarding the substance of the transaction itself. Do such actions not fall within the definition of price control then?

## Is it true that the tax authorities are not restricted in selecting the technique (method) for determining the price?

Having recognised that tax inspectorates are not able to confine themselves to price control methods which are stipulated in the Tax Code, the Russian Supreme Court did not determine what the procedure should be for calculating the amount of an unjustified tax benefit[5] and what guarantees a taxpayer should have to protect it from the unlawful actions of tax authorities.

Given the imperative method that regulates the actions of tax authorities, whereby everything which is not expressly permitted by law should be prohibited, tax authorities act only within the scope of the powers granted to them by the legislature.

Today, the definition of market price and the mechanism by which tax authorities determine it is enshrined only in Section V.1 of the Tax Code. In our opinion, and for the purposes of determining the actual amount of a tax obligation when an unjustified tax benefit is obtained, a tax inspectorate may not step away from the rules for determining the market price, which are enshrined in the Tax Code.

If we acknowledge that codified methods of price control extend only to controlled transactions or transactions equivalent to them, we should inevitably make a conclusion concerning tax discrimination against taxpayers. There are guarantees and a clear mechanism of actions of the tax authorities for taxpayers that are parties to controlled transactions with respect to price control methods applied when determining actual tax obligations. If the issue at hand concerns transactions that fall outside the ambit of Section V.1 of the Tax Code, all the guarantees that the law establishes will be off the table. Instead, a tax authority will be free to determine the market price in whatever way it wishes. Such an approach may result in the tax authorities abusing their position.

## Conclusions

To determine actual tax obligations in lawsuits over an unjustified tax benefit, the rules enacted in the current legislation are sufficient. In the Minaevsky Business Centre LLC case, the panel should not have created new general rules for determining tax obligations based on the facts of the specific case.

If the dispute was over an unjustified tax benefit obtained by the taxpayer, the tax authority and the court should have consistently determined:

- the actual economic substance of the transactions consummated and the tax implications of such transactions which the taxpayer tried to avoid;
- the actual tax obligations under the transaction in fact consummated, based on the market prices of it.

The absence of special provisions in the Tax Code in relation to determining the amount of an unjustified tax benefit (owing to there being no statutory regulation of this concept) should not rule out the need to apply the methods set in Chapter 14.3 for determining the amount of such an unjustified tax benefit.

[4] "The tax authority had grounds for concluding that the interests of the public purse were violated by the taxpayer selling the property at prices that differed substantially from the market level." The transactions "were aimed at deriving a tax benefit on account of the tax base being misrepresented when the buildings were sold at a price significantly lower than the market price."

[5] No such criteria are enshrined in the Tax Code.

# Financing a Russian subsidiary: unexpected tax outcomes

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According to current Russian legislation[1], interest charged on borrowing of any kind is treated as an expense deductible for profits tax purposes, provided the requirements of article 269 of the RF Tax Code are observed. The rules may sound simple; however, in practice foreign investors face a number of obstacles when claiming profits tax deductions relating to interest expenses at the level of a Russian subsidiary. Additionally, the inability of a subsidiary to repay debt due to financial difficulties and the need for recapitalisation could also lead to profits tax exposure. This article addresses several issues that, if overlooked, could materially affect the tax efficiency of a subsidiary in Russia.

## Russian tax rules limiting the deductibility of interest expenses

Under current legislation[2], interest expenses with regard to the related parties' transactions are deductible if their level falls within the market interval or, if the maximum interval value is exceeded, corresponds to the market level. In the latter case the market level of interest should be justified, e.g. by referring to comparable uncontrolled transactions. If the parties to the transaction are not related, the interest rate agreed by the parties assumed to be in the market and the corresponding interest expense is fully deductible for profits tax purposes in the hands of the borrower.

However, taxpayers do not usually expect that in addition to the above criteria, the general deductibility principles of the RF Tax Code[3] such as economic justification of expenses and their relation to income generating activities should be fulfilled to enjoy profits tax deductions with regard to any accrued interest.

In particular, the deductibility of interest expenses could be successfully challenged by the tax authorities based on insufficient economic justification:

- where the Russian subsidiary deducted interest expenses on loans issued exclusively to refinance existing loans[4];
- where the shareholders loan was used to finance loss making activities (sale of shares with a loss)[5];
- where the company lent the borrowed funds to related parties, charging an interest rate that is lower than the interest payable to its creditor (thus, generating an unjustified loss on such financing activities)[6], etc.

[1] Sub item 2 of item 1 of article 265 of the Tax Code of the Russian Federation (hereinafter, the RF Tax Code).

[2] Item 1 of article 269 of the RF Tax Code (as amended effective 1 January 2015).

[3] Item 1 of article 252 of the RF Tax Code.

[4] The Supreme Court Ruling of 5 April 2016 N 305-KG16-1901.

[5] The Supreme Court Ruling of 20 June 2016 N 305-KG16-6055.

[6] The Supreme Court Ruling от 25 March 2016 N 308-KG16-991.

Consequently, in addition to observing the market interval for the interest rate, the subsidiary should follow the general deductibility principles and/or the financing arrangement itself should have economic merit to enjoy profits tax deductions relating to the accrued interest.

**Recommendations:** consider establishing the interest rate on shareholder loans within the stated market interval to avoid the need for excessive transfer pricing documentation supporting the market level of interest. Even if the market interval requirement is observed, be prepared to support the economic justification of interest expenses, in particular, by demonstrating that the borrowed funds are used to finance income-generating activities and the financing arrangement is not aimed at merely receiving an unjustified tax benefit.


## Russian thin capitalisation rules

The deductibility of interest expenses accrued by a Russian legal entity could be limited for profits tax purposes under thin capitalisation rules[7]. The amount of interest accrued on controlled debt which exceeds the limit (calculated by applying a 3:1 debt to equity ratio or 12.5:1 debt to equity ratio for certain financial institutions), should not be recognised as a deductible expense for profits tax purposes and should be treated as dividends.

Currently, the thin capitalisation rules could only be applied for controlled debt as defined in the RF Tax Code and could not be extended to any related party debt that does not fall under the definition of controlled debt[8].

However, starting 1 January 2017 the court may recognise any outstanding debt as controlled debt, if the final debt repayment recipients are affiliated entities, whose lending should be classified as controlled debt[9].

The upcoming changes effectively mean that the tax authorities could scrutinise the interest deduction on any intercompany loan if the interest payments could be viewed as hidden dividend distribution.

The provisions of the effective treaties on the avoidance of double taxation with the country of residence of the foreign lender could not provide the

[7] Item 2 of article 269 of the RF Tax Code.

[8] Although recent court practice supported the extension of controlled debt by including debts towards foreign subsidiary companies (e.g., see the Supreme Court definition of 29 February 2016 N 305-KG 15-20153).

[9] According to item 13 of article 269 of the RF Tax Code (effective 1 January 2017).


expected protection against such challenges, as the courts consistently rule on the priority of Russian thin capitalisation rules over the unlimited interest deduction provisions of the treaties[10].

**Recommendation:** consider the thin capitalisation rules each time the group companies (including foreign "sister" companies) are financing the Russian subsidiary. In case the debt-to-equity ratio could not be observed due to unfavourable market conditions, be prepared to forfeit profits tax deductions and pay withholding income tax with regard to interest repayments to foreign lenders at the tax rate set for dividends.

## Reclassification of intercompany debt into capital

Russian tax legislation contains neither criteria to classify shareholder loans into equity, nor specific provisions relating to the deductibility of interest on hybrid loans.

However, according to current court practice[11], the tax authorities could reclassify the shareholder's debt into equity.

The tax authorities could reach such a conclusion by proving that the parties to the loan agreement do not undertake actions aimed at the proper performance of their contractual obligations and the legal framework of a loan does not correspond to the actual economic substance of the transaction. In other words, these parties have business relations beyond the provision of the loan.

In particular, if the shareholder is not taking action to claim the interest payments from the subsidiary in a timely manner (or the loan repayment terms are not clearly stated) and/or the shareholder reduces the interest rates and plans to subsequently forgive the outstanding debt, the tax authorities could claim that the loan agreements in fact represent investments in the subsidiary's capital. In this case, the tax authorities could disallow the profits tax deductions relating to interest charged on such debt by the subsidiary for profits tax purposes.

**Recommendation:** establish market terms of intercompany loans and strictly observe repayment deadlines to avoid any doubts on the investment nature of the loan. If the subsidiary fails to meet the established debt and interest repayment schedule, consider

[10] Please refer to the Ruling of the Supreme Arbitration Court Presidium of 15 November 2011 N 8654/11 and a number of subsequent rulings (e.g., the Ruling of 7 December 2015 N 310-KG15-15757).

[11] See Definitions of the RF Supreme Court of 8 May 2014 N VAS-5243/14 and of 11. December 2014 N 305-KG14-5812.


charging penalty interest or novation of the loan obligation in a way that could be applied to an independent borrower.

## Tax implications of the subsidiary's debt cancellation

The parent could be willing to forgive or cancel the subsidiary's debts if the subsidiary is unable to repay them (because of poor performance or a dramatic increase in liabilities nominated in foreign currencies due to revaluation).

Current legislation states two tax efficient ways to cancel excessive shareholder debt, where income resulting from the debt cancellation in the hands of the borrower is exempted from profits tax:

**Option 1.** If a Russian legal entity receives property on a free-of-charge basis from its shareholder (participant), provided that the contributing participant is holding more than 50% in the recipient's share capital and the above property (except for cash) is not alienated within one year period[12].

**Option 2.** If a Russian legal entity receives property, property rights or other rights having monetary value from its shareholders (participants), including ones received in the form of cancellation of the debts payable to such shareholders (participants) in order to increase its net assets[13].

Notably, the first option is less favourable for taxpayers, as the debt forgiving parties are limited by the majority shareholders (participants) and the tax exempted forgiveness could only be enjoyed for the debt principal (as it corresponds to the contributed cash). The income relating to the forgiven interest could be viewed as a free-of-charge transfer of property rights (but not property) and consequently could not be profits tax exempt.

Under the second option, the tax-exempt debt forgiveness is possible for minority shareholders (participants) and the exemption is extended to the transfer of property rights. A textual analysis of the RF Tax Code suggests that under this option forgiveness of the accrued interest should also be exempted from profits tax. However, the RF Finance Ministry is arguing that accrued interest, if forgiven, is subject to profits tax and such a position was recently supported by the court. In this regard, the subsidiary could have an uncertain tax position relating to any accrued interest, if the parent decides to forgive the unpaid amount thereof in the course of its net assets increase.

**Recommendation:** consider the subsidiary repaying any interest accrued under intercompany debts, if the principal is forgiven by the parent in a tax-exempt way indicated above, to avoid additional profits tax obligations.

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Summarising the above, Russian tax legislation relating to interest deductibility is subject to interpretations by the tax authorities and the courts, sometimes in a very aggressive way, where the decisions are adopted by referring to the unjustified tax benefit doctrine, but not to the textual analysis of the tax legislation. In this regard, where a strategic decision regarding financing of a Russian subsidiary is taken, it is vital not only to precisely analyse the applicable tax law and court practice, but also to elaborate an economic justification of the planned transactions. The involvement of an external advisor with extensive experience in Russian tax could also help to structure the subsidiary financing in a tax efficient way.

[12] Sub-item 11 of item 1 of article 251 of the RF Tax Code.

[13] Sub-item 3.4 of item 1 of article 251 of the RF Tax Code.

# Intercompany services: what is the right price of the deal?

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With the globalisation of the world economy and companies doing business in diverse tax jurisdictions, profit shifting and the consequent claiming by national tax authorities of a larger share of profit has become an important issue.

In order to ensure the fair distribution of profit among different countries, the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ("OECD Guidelines") request recognition of all intercompany services from multinational companies (such as administrative and legal services, staff training, etc.) for tax purposes. To that end, the OECD Guidelines describe two principal approaches inside a multinational group of companies – a service agreement or a cost allocation.

In the meantime, the Tax Code of the Russian Federation ("Tax Code") does not recognise cost allocation and the only possible approach is an intercompany service arrangement. This entails the requirement to determine the appropriate level of service charges, taking into account the respective transfer pricing rules, i.e. considering costs incurred as well as a certain mark-up.

In its transfer pricing section the Tax Code does not set out any special rules for intercompany services and the determination of their arm's length price. So general transfer pricing rules should be observed, i.e. the most suitable method should be selected and justified in each and every case.

Overall, the OECD Guidelines recommend the comparable uncontrolled price (CUP) method or the cost plus (Cost+) method for the determination of an arm's length price for intercompany services. In general, the CUP method is certainly the best option, but it can only be applied where similar services are acquired from/rendered to independent parties or are available on the market (i.e. where information is available regarding comparable transactions). Otherwise, the remaining option is the Cost+ method (or the transactional net margin method as a less organic and more complicated alternative).

The Cost+ method is efficient due to its convenience for determining the service price other than in the fair market environment (i.e. where there are no bids/competition and where the subject of the services is exclusive in nature). This method is expected to determine the price mainly on the basis of the provider's internal information, i.e. the best available grounds in that case. This explains its popularity


in commercial practice, including in transactions between independent parties where transfer pricing is not an issue.

Additionally the Cost+ method is convenient for accounting purposes and attunes the taxpayer from the very start towards the confirmation of the nature of the services because the determination of expenses that make up the service price is a handy matrix for the description of the services to confirm their economic substance. This is extremely important in view of the recent claims of tax authorities and recent trends in court practice where the issue of economic substance is a point of significant contention between taxpayers and the authorities.

Notwithstanding the organic nature and convenience of Cost+, it is associated with certain tax risks and complexity in respect of its practical application.

• The Cost+ approach involves the determination of all cost items (including overheads) forming the basis of services. Consequently, where the service provider performs other activities and/or provides services to other companies inside/outside the group, the accuracy of the allocation of overheads to individual business lines/customers may be contested. The same concerns will also arise where certain direct expenses are related to more than one customer.

• The Tax Code states that for the Cost+ method the data presented in the financial statements and underlying computations of the net margins must be presented in a comparable way that mitigates the effect of accounting policy deviations on the profit margin. So the unique nature of the service gives rise to the same obstacle which hinders the application of the CUP method – the difficulty to find comparable companies and the lack of required data in their financial statements.

• A detailed presentation of the provider's expenses in primary documents will bring about the scrutiny of each item for relevance (economic feasibility) on the part of the tax authorities. Consequently, there is a risk of (a) a challenge of comparability of the companies for which gross margin was computed; (b) a challenge of documentary evidence of the expenses included in the service price.

To sum up, although the Cost+ method is associated with certain risks, nevertheless it remains the optimum method in the absence of comparable services on the market. The alternative – the transactional net margin method – involves similar risks and difficulties, while lacking the advantages of the former. In any case, recent court precedents have demonstrated that the highest risks as to intercompany services are entailed by their documenting and the confirmation of their economic justification and relevance for the customer. These risks can be minimised via properly formed primary documents. However, the latter may require additional human and financial resources and the associated expenses can outweigh the benefits from the provision of the services. Therefore, overall, intercompany service arrangements should be implemented with due care with respect to both pricing matters and transaction documentation, with a thorough consideration of all the pros and cons and care taken to avoid all the pitfalls well in advance.

# Tax control – new rules of an old game

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For a long time, tax crime cases were quite rare and most tax disputes were won by taxpayers, so little attention was paid to taxes as regards criminal matters.

But the last few years have seen the opposite: company tax dispute victories are becoming less and less frequent and the number of tax crime cases are increasing.

The government is obviously setting new rules of the game when it comes to taxes and is actively putting them into practice, so businesses must be aware of these changes and pay due regards to them in their operations.

## Tax bodies and courts take a new approach to tax audits and disputes

The way the Russian tax system is developing is also affecting the development of the tax control system, meaning the approach taken by the tax authorities to the performance of audits is changing rapidly.

Gone are the times when tax bodies tended to focus on inaccuracies and minor, technical errors in company documents.

Audits today are mostly aimed at dealing with specific significant and systemic issues, with auditors scrupulously gathering an impressive evidential base which goes far beyond formal arguments.

Information exchange between the tax authorities of different countries plays an important part in this and the Russian tax authorities are recently making more frequent and effective use of such exchanges.

There has been a sharp drop in the number of tax disputes heard by state commercial courts: from 24,554 in 2012 to 13,435 in 2015; a 45% decrease.[1] Not only is the number of tax disputes constantly falling, taxpayer victories are also becoming increasingly rare: in 2012, taxpayers won 61.8% of the cases, in 2013 – 57%, in 2014 – 54.4%, and in 2015 – 50.3%.[2]

At the same time, tax disputes are growing in complexity, rising from the amateur to the professional level. The main reasons are that the professionalism of tax officials is increasing rapidly and that the state commercial courts are tending to hand down anti- rather than pro-taxpayer rulings.

What do these changes mean for companies? Previously unnoticed carelessness and mistakes can now have serious adverse consequences for them.

[1] Statistics from the SCC RF (http://www.arbitr.ru/) and the Judicial Department of the SC RF (http://www.cdep.ru).

[2] Statistics from the SCC RF (http://www.arbitr.ru/) and the Judicial Department of the SC RF (http://www.cdep.ru).


## Tax wrongdoings are now more likely to attract prosecution, and management to be held personally liable for company tax debts

The law enforcement agencies are also playing a significant role in the creation of the new rules of the game. Since 2014, investigators have been able to act independently from the tax authorities. Remember how the powers of law enforcement agencies were restricted back in 2011, and cases could only be initiated following a tax audit? This is no longer the case, and investigators can have a tax view of their own.

It is of no surprise that the Investigation Committee of Russia (ICR) has announced a rise in the number of tax crime cases and in the amounts recovered by the treasury as a result.

The statistics show that from January to July 2015, 5,887 tax crimes were identified, with the respective figure for the same period in 2016 being 6,195[3]; so the law enforcement agencies are obviously becoming increasingly active when it comes to tax control.

These trends are illustrated by the growing numbers of high profile tax crime cases, such as the Sunrise Tour case: in September this year, the company CEO was sentenced to three years in a penal colony for not paying over RUB 650 million in taxes.[4]

Budget revenues from tax crime damages are consequently also going up: in just five months in 2015, the treasury recovered over RUB 5.5 billion, a 76.7% year-on-year increase.[5]

A major role in this increase is played by the legislative provisions, which

[3] Statistics from the General Prosecutor's Office of the Russian Federation (www.crimestat.ru).

[4, 5] ICR data (www.sledcom.ru).

release first-time offenders from criminal liability if they pay all the taxes, fines and penalties due (as calculated by the investigator). That was how the criminal case against the management of SU-155 was terminated after the company paid taxes of over RUB 2 billion.

Such tax revenues are also boosted by the rapid development of court practice confirming the possibility of recovering company tax debts from its management.

The foundations are currently being laid for a fundamentally new principle: personal, either criminal or other, liability of management not only for a company's activities but also its tax debts. Returning to the Sunrise Tour case, in addition to the CEO being held criminally liable, state commercial court rulings on recovering the company tax debt from him were upheld by the Supreme Court after consideration of the company's bankruptcy case.[6]

This all clearly demonstrates that the government is stepping up overall control over the payment of taxes. There now exist, once again, two basically different systems for controlling the payment of taxes: (1) tax audits, a system well known to most companies, the results of which are becoming increasingly difficult to challenge in state commercial courts and (2) law enforcement control supported by general jurisdiction courts issuing a negligible percentage of not-guilty verdicts; just 2% for white collar crimes.[7]

## How businesses should respond to the changing rules of the game

Given that the government is taking a fundamentally new approach to the recovery and administration of tax payments and company debts are increasingly often being recovered from their management, effective protection against tax risks and their management are becoming more important than ever before.

In tax disputes today, it is the facts and relevant evidence that are most important, while the formal part is retreating into the background, so cannot be counted on.

Unlike many other case categories, in tax disputes the courts primarily investigate the economic substance of the specific operations, rather than how they are formalised in legal terms and whether they formally comply with the effective legislation (the substance over form principle).

A successful outcome of a tax dispute consequently requires, in most cases, not only the most comprehensive and well elaborated approach at all stages but also the formulation of a legal position based on facts and evidence, far from being confined to legal arguments and legal literalness.

Competently elaborated defence tactics combined with an evidential base are largely of decisive significance for effective defence during criminal prosecution. Account must be taken of the way defence tactics might differ fundamentally in tax crime cases and tax disputes, with a do-it-yourself approach at any stage of the defence potentially having serious negative consequences. It is no secret that most in-house legal teams, be them experienced and competent, have no experience of criminal defence, especially when it comes to taxes, as their duties are totally different.

Considering the change in the rules of the tax game, never forget to do your homework carefully by tightening the requirements for the transparency of operations and paperwork, improving compliance procedures, elaborating and applying policies for working with business partners, all based on the available case law.

Ultimately, this will help to reduce the likelihood of the company violating the tax legislation and, particularly, evading taxes.

Focus especially on the most turbulent areas for the particular company which may be systemic or sectoral in nature.

From the criminal prosecution perspective, the greatest danger is posed by challenges to the actual existence of operations or the conditions for receiving tax advantages, especially when it comes to VAT recovery[8], such as:

- relations with bad faith counterparties;
- commercial operations within a single group (including cost sharing);
- failure by companies to fulfil tax agent obligations;
- concealment of property from taxation;
- use of tax benefits.

[6] Link to case: http://kad.arbitr.ru/Card/6a2c3963-214c-4117-b396-405754c061c3

[7] Statistics from the Judicial Department of the SC RF (http://www.cdep.ru).

[8] Breach of tax legislation connected with VAT recovery qualifies as fraud (not tax evasion) under the Russian Criminal Code and cannot be discharged by tax repayment.


Where to begin? Best start with prevention, rather than cure:

• pinpoint the riskiest areas/transactions: practice shows that the risks of tax prosecution are often not assessed at all;

• review the approaches taken (tighten control over) to selecting and concluding agreements with business partners;

• make sure that the nature and terms of work with counterparties complies with market conditions and the actual relations correspond to what the contract says;

• check existing contracts for availability of not just the requisite formal documents but also explanations of the purpose for any non-standard features, and of course evidence of delivery;

• make sure the company has documents signed by counterparties with demonstrably authentic signatures;

• check there is evidence that intra-group operations are real and that the prices of such deals correspond to their substance and scope;

• give staff the necessary training in both day-to-day work and liaison with the tax and law enforcement bodies, including when such situations arise suddenly.

If your company manages to pinpoint weak spots before the controlling bodies do, you must not wait in the hope that they will go unnoticed. It is better to use the time you have to minimise the identified risks: find out all the necessary facts, prepare additional evidence, and undertake any new steps required by the specifics of the situation. There is no universal defence solution, so each specific situation needs to be analysed in detail and an optimum strategy and tactics developed for defending your interests.

Despite all the complexity and, at first glance, difficulty involved in such a process, it is worthwhile because it will allow the company perhaps not to avoid, but at least to greatly mitigate the risks of additional tax being assessed, as well as those of criminal prosecution.

Remember, however, that quality prevention greatly reduces not only the risks themselves but also the scope of work and related costs in the future.

# Practical aspects of the implementation of electronic document flow

**MIKHAIL AKSENOV**
Tax Planning Analyst, Philip Morris Sales and Marketing

## Introduction

The processing of documents in electronic form (E-document flow or EDF) is a newly designed process, legally framed/regulated and promoted at the governmental level in Russia.

To be legal electronic documents should comply with effective legislation, including Federal Law No. 63-FZ "On the Electronic Signature" dated 6 April 2011. The law regulates the use of an electronic signature and distinguishes between three types:

**1.** simple electronic signature;

**2.** advanced unqualified electronic signature;

**3.** advanced qualified electronic signature.

The advanced qualified electronic signature is only one which is considered as an electronic equivalent to the handwritten signature and is associated with the respective legal consequences.

E-document flow is strongly recommended by government officials, including the tax authorities, for whom it provides the opportunity to decrease the huge quantity of printed documents provided by taxpayers during tax audits.

Moreover, tax law now stipulates certain cases in which the submission of documents to the tax authorities via electronic channels is mandatory:

- major taxpayers are obligated to submit all tax returns and statutory financial statements in electronic form and to ensure electronic receipt of the tax request; otherwise a bank account can be blocked by the tax authorities;
- VAT returns should be submitted in electronic format.

It will not be a big surprise if someday in the near future EDF will become mandatory for almost all taxpayers with the tax authorities.

Anticipating this change, which will have significant implications on systems and business processes, the process of transition to EDF should be a high priority project in any companies that want to be innovative and competitive.

However, there is no golden rule on how to implement EDF in a company, and it is always helpful to learn from the experience other companies have gained while implementing EDF.

In this article a number of practical issues are discussed that could be helpful for companies implementing EDF.

## How to start

First, you need to decide what the objective of the project is. As an example: "Extensive implementation of the electronic signature covering all processes where it is possible with the integration of EDF into the internal system".

Second, the project scope should be defined (internal document flow only or external, or both; with affiliates or with all counterparties, etc.). For instance, external EDF implementation in an international company which has a presence in Russia may be divided into three steps:

**1.** EDF between all Russian legal entities;

**2.** EDF between Russian legal entities and major domestic customers/suppliers;


**3.** intercompany cross-border transactions.

For each of the steps resources should be allocated (time, people, etc.) and a timeline should be drawn up.

Then, the processes "as is" and "as to be" should be described. Workshops/ interviews with all the involved departments will help to address this task.

## Practical aspects you need to pay attention to when implementing EDF

**1. Legislation**

Taking into account that EDF is relatively new in Russia, not all of the aspects of EDF are fully covered by legislation. So solutions should be developed by specialists from legal, tax and other departments. This should be considered before a project team is set up.

**2. Project team**

If there are no people solely dedicated to the project then the time to be spent by employees on everyday duties and tasks related to the project should be carefully allocated.

**3. Technical issues**

The speed of EDF implementation is dependent on the technical platform used in a company. There are EDF integration solutions for SAP, 1C and other systems. If the company uses a customised SAP solution then a lot of the adaptation of EDF integration software should be developed. This should be considered when allocating time and resources to the project.

**4. Electronic signatories**

If the company decides to use an advanced qualified electronic signature, then EDF potentially will require a significant number of such signatories for the staff involved. The process of obtaining them could be time consuming and it is better to do this at the planning stage.

**5. Staff training**

The success of EDF implementation depends on people. So special attention should be paid to guidelines and instructions. The most important is staff training where project team members discuss EDF and allow the new processes to be tested in a testing environment. The staff training should be planned in advance.

**6. "What if" situations**

A key point for successful EDF implementation is to control all possible malfunctions. The so called RACI model (R-responsible, A-accountable, C-consulted, I-informed) could help here. By using this model each stage of any process is linked to a particular person or department who is responsible and accountable for the stage, and who should be consulted with or informed by. This reduces uncertainty upon the implementation of a new process as all the parties involved know what to do.

## Conclusion

Recent developments in EDF and its promotion at the governmental level shows that EDF is not merely a nice-to-have tool but a tool that provides a competitive advantage.

The successful implementation of EDF depends on many factors. I would like to pay attention to the importance of the planning process. At this stage you need to consider: the objective of the project, its scope, the description of the processes "as is" and "as to be", practical aspects such as legislation gaps, who the project team members will be, what kind of technical issues related to the integration of EDF into the current accounting or ERP system need to be resolved, issues related to electronic signatures, staff training, dealing with "what if" situations.

Despite all the difficulties, it is possible to meet deadlines and achieve goals thanks to accurate planning.

# CEO liability for damages in tax crimes

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Now we can reasonably confirm that the number of "tax crimes", that is, taxpayer (a taxpaying company's CEO) charges on tax defaults, non-fulfilment of tax agent obligations and concealment of debtor assets in arrears recovery is on the increase[1]. This can be explained both by the overall trend towards the tightening of tax administration regulations and by the simplification of procedural arrangements for the initiation of criminal cases. The unfavourable forecast provided by the Tax Committee of the AEB in this regard has been fully confirmed[2]. The practice in various regions of the RF also shows that CEOs are coming into increasing contact with law enforcement agency representatives in connection with tax crime investigations. Based on the above, we believe that in evaluating the risks, CEOs should also take into account the increased probability of the application of criminal law sanctions relating to violations of tax legislation.

The law previously provided the opportunity to tax authorities to pass the company's tax debt onto its CEO. A suretyship agreement on the company tax debt as well as bankruptcy arrangements provided by the law were used for this purpose. In this article, we try to highlight a completely new way of passing the debt burden from the company as a whole onto its CEO individually.

Obviously, criminal prosecution of a company's CEO for non-payment of debts is a major upheaval, and a shock for any CEO. Such an outcome of a tax dispute is the worst possible for a taxpayer even considering that, in this case, Russian courts usually either apply sanctions that do not involve prison sentences or pass a suspended sentence. However, some of the latest proceedings relating to tax crimes have led to a new trend, unfavourable for taxpayers. According to this trend, an additional obligation may be placed upon a taxpayer's CEO, guilty of committing a tax crime, to personally pay for the damages incurred. At the same time, the taxpaying company is not released from the obligation to compensate for tax arrears, that is, the debt owed is actually doubled.

The RF Code of Criminal Procedure allows damage incurred by a criminal to be recovered in favour of the affected party by filing a "civil action in a criminal case". The Supreme Court of the RF, and the Russian Prosecutor-General's Office typically insist on using this method in order to effectively recover victim losses.

The problem described above has become relevant because the state budget of the RF is the party affected by the criminal non-payment of taxes. Therefore, compensation of damages incurred through non-payment of taxes should actually be reduced to the payment of the appropriate tax amount and a penalty for the overdue

[1] Statistical information is available at the website of the Russian Prosecutor-General's Office http://crimestat.ru/analytics.

[2] See European Business in Russia: Position Paper 2014. p. 265 http://www.aebrus.ru/upload/iblock/ded/aeb_pp_lr.pdf


tax payment. The tax and penalty amounts should be determined based on the RF Tax Code.

However, in considering criminal cases of tax crimes in 2014–2015, the courts repeatedly adopted the decision that compensation of damages incurred by a tax crime recovered from the tax avoiding company's CEO is an amount in no way related to the amount of the company's debt. Therefore, the CEO shall pay "damage compensation" following the rules provided by the RF Criminal and Civil Code and the company shall compensate the tax arrears determined following the rules provided by the RF Tax Code. This means that the total tax debt of the company is actually doubled from the start and partially becomes the CEO's responsibility.

The most vivid examples of these legal actions, in our opinion, are Ruling No. 81-КГ14-19 of the Supreme Court of the RF in 2015, Ruling No. 3-УДп14-2 of the Supreme Court of the RF in 2014, Ruling No. 33-18581 of Moscow City Court in 2014, Ruling No. 33-37650 of Moscow City Court in 2014, and Ruling No. 44У-23 of the Kurgan region court in 2016. For all of the above cases, the courts decided to satisfy civil lawsuits on the recovery of damages incurred by the tax crime from the company executives without analysing what would become of the main tax debt of the company itself. The courts highlighted that they applied only the regulations of the RF Code of Criminal Procedure and RF CC and did not apply tax regulations to the specific situation because the recovery of tax arrears and compensation of damages incurred by the tax crime were different legal procedures. General jurisdiction courts believe that tax arrears are covered by public law and the compensation of damages incurred by a tax crime should be recovered under private law.

Despite the obvious logical and economic inconsistencies of this approach, the RF Constitutional Court acknowledged that this practice of applying and interpreting the law complies with the Constitution[3], which means that the described practice will be applied further.

This approach used by the courts to examine criminal activity in regards to tax crimes not only leads to an additional financial burden on the persons found guilty of tax crimes by the courts, but also makes it difficult to implement the company executive's right to be released from criminal responsibility by settlements until legal proceedings are initiated. Law enforcement agency officials believe that the guilty party should pay the damages incurred to the state budget in person in order to be released from responsibility and the company managed by the guilty party should pay the debts itself. So it is evident that it is required to pay the same debt twice at the risk of the initiation of criminal proceedings.

We believe that this course will lead to an additional financial burden on the taxpayer, which is unacceptable. We believe that in the situations described above, apart from standard defence practice, the attorneys of the accused parties should demand that in the case of a conviction and a decision to satisfy the civil action, the court should not only specify the total amount of damages to be compensated but the specific debt, its amount and the timeframe in which the convicted party should pay compensation. We think that this would prevent double payment of the same debt to the state budget.

[3] Ruling of the RF Constitutional Court from 2015 N 2731-O.

# Developments in judicial practice in tax disputes

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While before 2015 judicial challenges were recognised by everybody as the most effective tool in Russia for tax dispute resolution in terms of quality, speed, openness, and general professionalism, since mid 2015 its position has been slipping away. By an "amazing" coincidence, the start of the negative trend coincided with the beginning of Russian judicial reforms in 2014 that led to the disappearance of the RF Supreme Arbitration Court and the subordination of the commercial courts to the RF Supreme Court.

The number of court disputes won by taxpayers continues to fall, along with an overall reduction in the number of tax disputes reaching the commercial courts. In 2014, the commercial courts considered 15,452 taxpayer claims for the invalidation of non-regulatory acts of the tax authorities, of which 8,411 claims, or 54% (approximately, with the proviso that a win did not always mean all claims being granted) were satisfied. In 2015, this was down to 50% (6,756 claims out of 13,435 filed in court). The official statistics for 2016 will only be available in 2017, but it is already apparent that the number of taxpayer claims satisfied will continue to fall, and perhaps significantly.

In our view, which is also based on our personal experience, these figures do not only indicate that it is becoming ever harder for businesses to seek the truth in disputes with the state in the courts, they also show that there is a clear shift of emphasis in resolving disputes between businesses and the FTS of Russia from the courts to the pre-trial stage. Most disputes are settled at the level of the FTS of Russia, if not the regional departments of the Federal Tax Service – from our own successful experience we can say that complaints sent there are reviewed thouroughly and their claims often satisfied, so there is no reason to look down on this procedural tool, which requires no additional expense (no state duties, no copying of documents).

These factors also play a role in the formation of court statistics: following the example of their colleagues in many developed countries, the FTS of Russia is clearly aiming to go to court only in cases it is sure of winning, or which are methodologically significant cases intended to reinforce new or existing doctrines for combating tax

evasion, and in which all decisions are usually adopted in favour of the state. Clear examples are the "beneficial owner" doctrine (MDM-Bank, BancaInteza, TELE-2 cases), and cases involving price manipulations to reduce taxes (StavGazOborudovaniye, Minayevsky cases). An exception is the eternal category of disputes concerning fly-by-night companies, which are still numerous despite following the general downwards trend.

However, it is also sadly true that judges display a "pro-fiscal" attitude to taxpayers, which adds to the gloomy picture. There is also an observable tendency (not clearly consistent with the principles of justice, to say the least) explicable in view of the difficulties forming the income side of the state budget: the larger the amount involved in the dispute, the lower the chances of winning. In judicial practice this year it is practically impossible to find a tax dispute over more than RUB 500 million that the taxpayer has won.

There are also "dangerous" transaction categories, where the changes of winning a dispute concerning the tax consequences are significantly lower than in others. When conducting any transaction or operation that gives rise to the right to a significant VAT refund (such as a real estate purchase), a taxpayer must be prepared for the significant difficulties defending that right in court, even if the transaction took place between completely independent, law-abiding, and transparent companies, and no legal violations were committed during the deal. Another dangerous category that is particularly relevant for Russian operating companies of foreign businesses is cross-border payments from Russia to foreign recipients, especially in the form of fees for services (the Oriflame Cosmetics, British American Tobacco, and Equant cases). Russian tax law does not recognise cost sharing agreements, as a result of which the Russian subsidiaries of multinational corporations often mask their participation in the apportioning of head office costs as payments for various services. These payments typically have the same effect on the tax authorities as a red cape does on a bull. The courts are highly concerned about such payments – the latest OECD reports (which are also used fairly tendentiously) provide further reasons to treat such payments as an erosion of the tax base and tax-free operating profit shifting from Russia.

One more dangerous category is regional tax benefits for investors (e.g. the Volkswagen, Peugeot-Citroen, and Avtotor cases). Despite the assurances of full support given by regional and local authorities when attracting the investor, in later stages, once the investments have been made, they tend to forget their assurances. Tax inspectorates – which are federally subordinated, typically look for any excuse to strip or limit an investor's right to the promised benefits when cases concerning investor rights to promised tax benefits go to trial. When a case reaches court they often succeed in doing so, partly due to the poor quality of regional legislation and the insufficient attention paid to it by the investor.

It also has to be said that the RF Supreme Court does not perform its functions as the regulator of judicial practice in tax disputes in the same way the RF Supreme Arbitration Court did – the total number of tax cases it reviews each year is very low compared to the RF SAC. This results in the absence of any kind of consistency in the way judges approach identical legal problems, going as far as directly contradictory judgments, sometimes even in the same court (e.g. cases concerning airlines applying the right to deduct the VAT paid for airport services). This "diversity" is exacerbated by the reduced appeal and cassation court activity – they have become extremely reluctant to overturn the decisions of lower courts, especially those in favour of the state.

The absence of effective supervision by the highest court instance is leading to breaks in practice – courts are beginning to revise their own apparently strong positions to the detriment of taxpayers. An example is the Parexel case (No. A40-194412/15), in which the Moscow Arbitration Court ruled that the performance of clinical studies in Russia by a pharmaceutical company was activity creating a permanent establishment, despite the existence of judgments on the same issue with directly contradictory conclusions.

What can we advise in these circumstances? In our view, taxpayers should now do everything to settle disputes in the pretrial phase. The time when the commercial courts could be counted on as a general purpose "saviour" from tax inspector abuses has gone. Naturally, this does not mean that it is pointless to go to court in any case, but it is not worth making it the keystone: it may turn out that reaching a compromise with the tax authority is a far more effective solution in the end. Court should be the last resort and not the focus in a dispute.

# AEB News

## Philippe Pegorier awarded the Order of Friendship

On 24 October 2016, Philippe Pegorier, Member of the AEB Board, Chairman of the AEB Machine Building & Engineering Committee, was awarded the Order of Friendship, the highest Russian award for foreigners, by the Russian President for his contribution to the development of business relations, economic and humanitarian cooperation with the Russian Federation as the Chairman of the AEB Board (2014–2016) and President of Alstom in Russia.

L–R: **Alexander Shokhin**, President of the Russian Union of Industrialists and Entrepreneurs (RSPP); **Philippe Pegorier**, Member of the AEB Board, Chairman of the AEB Machine Building & Engineering Committee, Alstom Russia; **Sergey Lavrov**, Minister of Foreign Affairs of the Russian Federation.

Sergey Lavrov, Minister of Foreign Affairs, presented the award in the name of the President of the Russian Federation.

The corresponding Decree was signed by Vladimir Putin on 4 August 2016 and published on 5 August 2016.

The Association of European Businesses is very proud as this award can be also seen as recognition of AEB merits.

## AEB Board holds a working meeting with Vygaudas Usackas

On 10 October 2016, AEB Board members led by Dr. Thomas Staertzel, Chairman of the AEB Board, and Dr. Frank Schauff, AEB CEO, held a working meeting with the Head of the European Delegation to the Russian Federation, Ambassador Vygaudas Ušackas, in his residence in Moscow.

L–R: **Teodora Ivanova-Staykova**, EU delegation to Russia; **Mariusz Salnikov**, EU Delegation to Russia; **Philippe Pegorier**; Member of the AEB Board; **Thomas Staertzel**, Chairman of the AEB Board; **Cesare Biggiogera**, Member of the AEB Board; **Filippo Baldisserotto**, Member of the AEB Board; **Olga Bantsekina**, Deputy Chairperson of the AEB Board; **Frank Schauff**, AEB CEO; **Vygaudas Usackas**, Head of the EU delegation to Russia; **Gerald Sakuler**, Member of the AEB Board, AEB Treasurer; **Alexander Liberov**, First Deputy Chairman of the AEB Board; **Teemu Helppolainen**, Member of the AEB Board; **Paul Bruck**, Member of the AEB Board; **Luis Portero**, EU Delegation to Russia.

L–R: **Natalia Zubarevich**, Independent Institute of Social Policy; **Tom Adshead**, COO, Macro-Advisory Ltd.; **Evgeny Gavrilenkov**, Higher School of Economics; **Stuart Lawson**, Chairman of the AEB Finance & Investments Committee, Executive Director, EY; **Frank Schauff**, AEB CEO.

## Talks on the Russian Economy

On 11 October 2016, the AEB held its third in the series "Talks on the Russian Economy", entitled "How to balance budget constraints with delivering a new normal". The event gave the audience an opportunity to hear updates from, and the thoughts of, the well-known experts who had been invited. They included Evgeny Gavrilenkov, Higher School of Economics, Tom Adshead, Macro-Advisory Ltd., and Natalia Zubarevich, Independent Institute of Social Policy. Participants could discuss with them the forecasts for the Russian economy, the structure of federal and regional budgets, factors affecting the current economic crisis, the influence of oil prices, the investment climate, consumption, and related topics.

The event was moderated by Stuart Lawson, Chairman of the AEB Finance & Investments Committee, EY. The welcome speech was made by Frank Schauff, AEB CEO.

## InRussia-2016 Conference

On 14 October 2016, the international business conference InRussia-2016 took place in Moscow at Swissotel Krasnye Kholmy.

The Association of European Businesses is regularly a partner of the conference. Frank Schauff, AEB CEO, made a welcoming speech at the conference opening.

During the plenary session the AEB was also represented by Philippe Pegorier, Member of the AEB Board, Chairman of the AEB Machine Building & Engineering Committee, President, Alstom Russia.

Among 350 delegates there were representatives from 50 regions of Russia and 18 countries, including Japan, Belgium, Italy, Turkey, France, Germany, Singapore, Romania, Slovenia and others.

The Russians were represented by Georgy Kalamanov, Deputy Minister of Industry and Trade, Igor Koval, Head of the Department of Investment Policy of the Ministry of Economic Development of the Russian Federation, Administration of the Fund of Industrial Development, Technological Development Agency, "Business of Russia", heads of regional development corporations, industrial parks, and also largest service and production companies.


Participants of the panel session

Frank Schauff focused on the issues of parallel importation and other related questions.

More news and photos can be found on the website of the association of industrial parks of Russia – AIP (organiser of the conference): http://www.indparks.ru/.

L–R: **Klaus Bräunig**, Managing Director, VDA – Germany; **Joerg Schreiber**, Chairman of the AEB Automobile Manufacturers Committee, President and General Director, Mazda Motor Rus; **Matthias Wissmann**, VDA – Germany; Yong-Geun Kim, KAMA- Korea; Dr. Frank Schauff, AEB CEO; Christian Peugeot, Chairman, CCFA.

## OICA General Assembly meeting

On 19–21 October 2016, the AEB took part in events organised as part of the Annual General Assembly meeting of the International Organisation of Motor Vehicle Manufacturers (OICA) http://www.oica.net/.

The meeting took place in Moscow for the first time in the Organisation's near 100-year history, and it brought together national automobile manufacturers/distributors associations from more than 20 countries.

Dr. Frank Schauff, AEB CEO, and Joerg Schreiber, Chairman of the AEB Automobile Manufacturers Committee, President and General Director, Mazda Motor Rus, attended the roundtable discussion devoted to regulatory issues connected with automated driving.

The participants paid special attention to the situation in the world's automobile markets. The status of the Russian market, and government support measures for it, were described by Alexander Morozov, Deputy Minister of industry and Trade of the Russian Federation.

During the meeting Yong-Geun KIM, (KAMA – Korea), the outgoing President of OICA, handed over his responsibilities to Matthias Wissmann, (VDA – Germany), the newly elected President.

Dr. Thomas Staertzel, Chairman of the AEB Board, delivered a welcome speech to OICA members at the Gala dinner which followed the GA meeting.

The AEB believes that this international event helped to bring the Russian automotive industry and market up to a new and higher level.

## Fifth Eurasian Forum in Verona

On 21 October 2016, Frank Schauff, AEB CEO, participated in the session "Innovation infrastructure in Greater Eurasia" as part of the Fifth Eurasian Forum that took place in Verona, at the Palace of the Gran Guardia (Palazzo della Gran Guardia). The Forum was organised by the Association Conoscere Eurasia and the Roscongress Foundation with information support from the AEB.

Among the key speakers at the session were Gregorio De Felice, Chief Economist of Intesa Sanpaolo Group, Chen Ning, Executive Chairman of ITTN, Alberto Mazzola, Head of International Affairs of Ferrovie dello Stato Italiane, and others.

The main subjects of the forum were the geopolitical processes in greater Eurasia, and innovation as a result of everyday creativity. Within these topics the participants discussed the key issues in economics, finances, energy, geopolitics, innovative infrastructure, agriculture and agribusiness. Special attention was attached to the new approaches to economic cooperation in conditions of global crisis, and to interregional cooperation.

The Forum traditionally brings together key representatives of the public authorities and business community of Russia, Italy, Azerbaijan, Armenia, Belorussia, Germany, India, Kazakhstan, China, France and South Korea.


**Frank Schauff,** AEB CEO


**Sergey Lavrov**, Minister of Foreign Affairs of the Russian Federation

## Briefing by Sergey Lavrov

On 25 October 2016, Sergey Lavrov, Minister of Foreign Affairs of the Russian Federation, briefed AEB members on the topic "EU-Russia relations in a changing world". The briefing took place at the Four Seasons hotel in Moscow.

The event was opened by Dr. Thomas Staertzel, Chairman of the AEB Board, and moderated by Dr. Frank Schauff, AEB CEO. The briefing was followed by a question and answer session.

The event was well attended by the representatives of federal and global mass media including worldwide TV channels.

A photo report is available on the AEB Facebook page.

## Presentation of the Altai Krai

On 26 October 2016, Alexander Karlin, Governor of the Altai Krai, made a presentation on the investment potential of the region to AEB members. The event was opened by Olga Bantsekina, Deputy Chairperson of the AEB Board, and moderated by Frank Schauff, AEB CEO.

The projects highlighted at the meeting were in tourism and recreation, agribusiness, food production and processing, machine-building and biotechnology. The event took place at the AEB Conference Centre.

A photo report is available on the AEB Facebook page.

**Alexander Karlin**, Governor of the Altai Krai

## Briefing by Gabriel Di Bella

On 2 November 2016, the AEB held a briefing with Gabriel Di Bella, Resident Representative of the International Monetary Fund in the Russian Federation, titled "Russia: From Stabilisation to Growth".

Annett Viehweg, Chairperson of the AEB Banking Committee, Chairperson of the Board, Deutsche Bank, Stuart Lawson, Chairman of the AEB Finance & Investments Committee, Executive Director, EY, and Frank Schauff, AEB CEO, moderated the event. The briefing was followed by a questions-and-answers session.

A photoreport can be found on the AEB Facebook page.

**Gabriel Di Bella**, Resident Representative of the International Monetary Fund in the Russian Federation

On 3 November 2016, at the opening session of the VI AIDA (International Insurance Law Association/Association Internationale de Droit des Assurances) Europe Conference in Vienna, Frank Schauff, AEB CEO, delivered a welcome address. AIDA is a non-profit making international association, formed in 1960, for the purpose of promoting and developing at an international level, collaboration between its members with a view to increasing the study and knowledge of international and national insurance law and related matters. The AEB (represented by the AEB Insurance & Pensions Committee) joined AIDA this year as the AIDA National Chapter in Russia.

## World Bank Briefing

On 11 November 2016, the Association of European Businesses (AEB) organised the World Bank briefing based on the World Bank Russia economic report #36.

The event was kindly hosted by the British Embassy at the residence of the UK Ambassador in Moscow and was chaired by Frank Schauff, AEB CEO, and Ian Proud, Economic Counsellor, British Embassy Moscow.

Apurva Sanghi, World Bank's Lead Economist for the Russian Federation, was a keynote speaker.

**Apurva Sanghi**, World Bank's Lead Economist for the Russian Federation.

## AEB meets Robert-Jan Smits, Director-General of DG Research & Innovation at the European Commission

On 11 November 2016, Robert-Jan Smits, Director-General of DG Research & Innovation at the European Commission, met the Association of European Businesses.

The aim of the meeting was for Mr. Smits to learn not only about the views of European businesses on the general economic climate in Russia but also to hear about the prospects of developing research & innovation focused cooperation, utilising Europe's and Russia's intellectual and scientific capital and technological complementaries. Companies also discussed with Mr. Smits the general framework conditions for carrying R&D activities in and with Russia.

L–R: **Gediminas Ramanauskas**, Policy Officer, European Commission; **Iskra Reic**, Vice President, Astra Zeneca; **Philippe Pegorier**, Member of the AEB Board, President, Alstom Russia; **Robert-Jan Smits**, Director-General, DG Research & Innovation, European Commission; **Frank Schauff**, AEB CEO; **Vygaudas Ušackas**, EU Ambassador to the Russian Federation, Head of EU Delegation to Russia; **Rene Pischel**, Head of European Space Agency; **Richard Burger**, Head of S&T and other EU Policies Section, EU Delegation to Russia.

## Briefing by Lev Kuznetsov

On 15 November 2016, members of the Association of European Businesses (AEB) had an opportunity to meet Lev Kuznetsov, Minister of North Caucasus Affairs of the Russian Federation, in Moscow at the Conference Hall of Ararat Park Hyatt.

Dr. Thomas Staertzel, Chairman of the AEB Board, opened the meeting with a welcoming speech. He noted that the North Caucasus region is quite attractive for foreign investors. Frank Schauff, AEB CEO, moderated the meeting. He said about close relations between foreign companies and regional administrations.

During the briefing Mr. Kuznetsov spoke about possibilities of investments and economic and trade cooperation with the North Caucasus region. The briefing was followed by a Q&A session. Representatives of AEB members companies received answers to their most pressing and important questions directly from the source.

**Lev Kuznetsov**, Minister of North Caucasus Affairs of the Russian Federation

## Localisation of production in Russia special investment contracts and other instruments of state support

On 15 November 2016, Frank Schauff, AEB CEO, took part in the Conference "Localisation of production in Russia: special investment contracts and other instruments of state support". The Conference was organised by the Russian Union of Industrialists and Entrepreneurs and Vegas Lex company. The Conference aimed to discussing and analysing benefits and constraints related to the Russian localisation policy for business. Frank Schauff presented an evaluation of the mechanism of special investment contracts from the perspective of foreign investors in Russia.

## Presentation of the Sakhalin region

On 16 November 2016, Oleg Kozhemyako, Governor of the Sakhalin region, presented the investment potential of the region to AEB members.

The event was opened by Olga Bantsekina, Deputy Chairperson of the AEB Board, and moderated by Frank Schauff, AEB CEO. The projects presented at the meeting were in tourism, hotels and recreation, agribusiness, food production and processing. The event took place in AEB Conference centre.

L–R: **Olga Bantsekina**, Deputy Chairperson of the AEB Board; **Dmitry Nesterov**, Deputy Head of the Government of the Sakhalin region; **Oleg Kozhemyako**, Governor of the Sakhalin region.

# AEB COMMITTEE UPDATES

## Banking Committee

On 13 October 2016, the AEB Banking Committee met representatives of the Central Bank (Department of Banking Regulation and Banking Supervision Department), to discuss issues related to the Central Bank's Instruction 154-I "On order of evaluation of remuneration system in a credit institution and procedure for sending the order to eliminate violations in its pay system to a credit institution" dated 17.06.2014.

## Customs & Transport Committee

On 15 November 2016, the AEB Customs & Transport Committee held a joint round table on customs issues with JETRO (Japan External Trade Organisation) and JBC (Japanese Business Club). The event was co-moderated by Dmitry Cheltsov, Chairman of the AEB Customs & Transport Committee, reported about the Committee's activities and Akihiro Okutake, Chairman of the JBC Customs Committee, presented the results of JBC's survey on customs issues. Wilhelmina Shavshina, Legal Director, Head of Foreign Trade Regulation Practice, DLA Piper, spoke about customs authorities' approaches to the requirements of HS codes classification and customs value adjustments. Yanina Tokadi, Business Development Manager, FM CUSTOMS, gave a presentation on customs value of the imported used goods. Julia Hertel, Head of Customs Department, IKEA, briefed the participants about turkish goods import complications. Yury Kiselev, Deputy GR Director, Renault Russia, reported on the advantages of authorsed economic operator status. The presentations were followed by a Q&A session.

L–R: Participants of the meeting

## HR Committee


L–R: **Tatiana Baskina**, Chairperson of the AEB Recruitment Subcommittee, Deputy Director General, ANCOR; **Vladimir Rora**, General Manager, Experium; **Arik Akhverdyan**, Founder, VCV; **Natalia Kulkova**, HR Director, Antal Russia.

On 19 October 2016, the AEB HR Committee held an open event entitled "Digital HR: In Transformation?" which was organised by the Recruitment Subcommittee. Participants exchanged views on the following topics: digital benefits cases, the benefits of the use of a corporate messenger, and predictive hiring based on big data. The speakers' presentations were followed by the experts' panel discussion. The panellists discussed the reality of digital HR: humans and robots, foresight and technological trends. The event was moderated by Tatiana Baskina, Chairperson of the AEB Recruitment Subcommittee, Deputy Director General, ANCOR.

## Machine Building & Engineering Committee

On 9 November 2016, the AEB Machine Building & Engineering Committee organised a meeting with Valentin Gapanovich, Senior Vice President, RZD.
Philippe Pegorier, Member of the AEB Board, Chairman of AEB Machine Building & Engineering Committee, President, Alstom Russia, delivered a welcoming speech. He pointed long-term collaboration between AEB member companies and RZD. Frank Schauff, AEB CEO, moderated the meeting.
Mr. Gapanovich told about energy saving and energy efficiency problems in the railway transport. He mentioned integrated programme of innovation of RZD Holding to 2020, as well as a developing high-speed transport in Russia.

L–R: **Philippe Pegorier**, Member of the AEB Board, Chairman of AEB Machine Building & Engineering Committee, President, Alstom Russia; **Valentin Gapanovich**, Senior Vice President, RZD; **Frank Schauff**, AEB CEO.

He also paid a special attention to the new Moscow Ring Railway.
The meeting was followed by a questions-and-answers session.

## North-Western Regional Committee


L–R: **Filippo Baldisserotto**, Chairman of the AEB Real Estate Committee; **Andrey Hitrov**, Chairman of the Construction and the Real Estate Subcommittee of the AEB North-Western Regional Committee.

On 6 October 2016, the AEB North-Western Regional Committee's Construction and the Real Estate Subcommittee held the open event "The outlook and medium-term forecast for the development of the Russian construction and real estate market, in particular in St. Petersburg: building bridges or walls?".

The event was devoted to the general economic situation and forecasts, and in particular to an overview of the construction and real estate market in Russia and the North-Western Region. A summary of the results for the first six months in the commercial real estate and construction markets (office, warehouse and commercial real estate) was provided by JLL. Besides this, different future forecasts for the market from the point of view of developers and construction companies were articulated. A thorough presentation of the main changes to legislation in the mentioned fields was presented and discussed. Well-known companies such as Danske Bank, JLL, YIT, EKE-Group, VTB Development, and others were invited to share their views and experience. The presentations were followed by lively discussions.
The event was kindly hosted and supported by Egorov, Puginsky Afanasiev & Partners in St. Petersburg.

On 12 October 2016, the Customs, Transport & Logistics Subcommittee of the AEB North-Western Regional Committee jointly with the Legal & Tax Subcommittee held a meeting on "Topic issues of the customs value and other issues of customs administration". The event was mainly devoted to the new resolution of the Plenum of the Supreme Court of the Russian Federation on the application of customs law.

Mikhail Saushkin, Head of Customs Payments Department of the North-Western Customs Administration (SZTU), was invited to the meeting to clarify issues raised by the resolution regarding recovery and refund of overpaid customs payments. Other subjects relating to customs valuation disputes which were discussed included: conditions for applying the transaction value method; the procedure for carrying out additional inspections; allocating the burden of proof; the legal view of recovery of penalties and interest payments; and appeals against decisions and actions of customs officials.

Such companies as Nissan, Group SEB Vostok, Ford Sollers Holding LLC, Port Hamburg, Ariston Thermo, Siemens Gas Turbine Technologies, DLA Piper, Beiten Burkhard, Rödl & Partner, Alinga Group and others participated in the meeting, asked questions of the representative of the SZTU and shared their practical experience.

The event was kindly hosted and supported by DLA Piper in St. Petersburg.

Speakers of the event

On 9 November 2016, the AEB North-Western Regional Committee's HR & Migration Subcommittee held a meeting on "Labour Inspection Audit, Redundancy and Summary Dismissals: Practical cases".

Olga Frolova, Chief Labour Inspector, Head of Labour Security Department of Labour Inspection of St. Petersburg, and Olga Gorokhova, Chief Labour Inspector, Head of Legal Issues Department of Labour Inspection of St. Petersburg, were invited to the meeting to brief on practical cases on main process of planned and unplanned inspection, identification of violations in the sphere of labor protection.

Such companies as LLC IKEA DOM, Heidelbergcement, Truck Production RUS LLC, Jungheinrich Lift Truck OOO, EPAM, SCHNEIDER GROUP, EY, Beiten Burkhardt, Rödl & Partner, Alinga Group, TMF-Group, Coleman Services and others participated in the meeting, asked questions to the representative of the labor Inspection and shared their practical experience.

The event was kindly hosted and supported by Baker & McKenzie office in St. Petersburg.

L–R: **Olga Frolova**, Chief Labour Inspector, Head of Labour Security Department of Labour Inspection of St. Petersburg; **Olga Gorokhova**, Chief Labour Inspector, Head of Legal Issues Department of Labour Inspection of St. Petersburg.

On 15 November 2016, the AEB North-Western Regional Committee held Baltic Breakfast Meeting on "B2B vs. B2C Markets – Consumer Behavior and Challenges".

The event was mainly held for companies from the Baltics to discuss the issues of consumer sales in Russia, B2B and B2C consumer behaviour trends in different sectors and the methods used to increase sales in Russia. Also, the event was aimed at analysing the ways the AEB could support the companies with information, lobbying opportunities, as well as other services and valuable benefits.

Such companies as YIT, H+H International A/S, Leipurin, Bank of Saint Petersburg, Allianz IC OJSC and others were invited to share their experience. The event provided a lively platform for discussion and exchange of practical experience, concerns and proposals. The event was kindly hosted and supported by the Consulate General of Finland in St. Petersburg.

Panel session

## PR & Communications Committee

On 7 October 2016, the AEB PR & Communications Committee held an open event: "Meeting at the State Tretyakov Gallery".

Tatiana Mrdulyash, Deputy Director General on Development, State Tretyakov Gallery, delivered a presentation on the museum's current activities and plans, and on opportunities for cooperation and partnership. The presentation was followed by a Q&A session. The participants of the event had the opportunity to visit the exhibition "The Golden Map of Russia".

**Tatiana Mrdulyash**, Deputy Director General on Development, State Tretyakov Gallery

## Product Conformity Assessment Committee

L–R: **Sergey Migin**, Deputy Head of the Federal Service for Accreditation; **Oksana Mezenceva**, Deputy Head of Department on Technical Regulating and Standardisation, Federal Agency on Technical Regulating and Metrology; **Andrey Polozkov**, Head of Accreditation and Harmonisation of State Control Division, Technical Regulation and Accreditation Department, Eurasian Economic Commission; **Alexej Soldatow**, Chairman of the AEB Product Conformity Assessment Committee, BSH Bytowyje Pribory; **Dmitry Patrakov**, Head of Department of International Cooperation in the field of Technical Regulation, Ministry of Industry and Trade of the Russian Federation.

On 8 November 2016, the AEB Product Conformity Assessment Committee held its Conference titled "Technical Regulation and Conformity Assessment in the EAEU and the EU: Prospects for Approximation". The event was opened by Frank Schauff, AEB CEO, and moderated by Alexej Soldatow, Chairman of the AEB Product Conformity Assessment Committee, Technical Regulation Manager, BSH Bytowyje Pribory. The key issues of the discussion were product conformity assessment, market surveillance, accreditation, safety and energy efficiency aspects, practical application of the technical regulations of the Customs Union and the EAEU, technical barriers, and its comparison to similar regulation of EU. The AEB sincerely thanks for sponsoring the event:

B/S/H/

The photoreport can be found on the AEB Facebook page.

## Safety, Health, Environment & Security Committee

On 14 October 2016, the Security Subcommittee of the AEB Safety, Health, Environment & Security Committee held a Round Table "Modern Cyber Trends & Threats".
The topic of cyber security is one of the most hotly discussed around the world. Targets for cyber-attacks are not only financial institutions but could be any business or individual, regardless of what they do. Ilya Sachkov, Founder and General Director, Group-IB, shared his vast knowledge and practical experience in cyber security. The event was moderated by Dmitry Budanov, Chairman of the Security Subcommittee of the AEB Safety, Health, Environment & Security Committee, CEO, Elite Security Holding Company.

**Ilya Sachkov**, Founder and General Director, Group-IB


## Small & Medium-Sized Enterprises Committee

On 9 November 2016, the AEB SME Committee held its open event "Sharing Best Practices in Solving Regulatory Changes" in a business breakfast format.
The participants of the event discussed the following topic issues: recent amendments to the trading law-areas from tax and legal sides; regulations on compulsory bankruptcy of a company for non-profitable business activities; labour and fire safety rules in Russia.

L–R: **Pavel Novikov**, Senior Associate, Baker & McKenzie; **Orlin Efremov**, Chairman of the Small & Medium-Sized Enterprises Committee, Managing Partner, Performance Partners LLC; **Alexey Malenkin**, Partner, CIS TARAS Leader, Tax & Legal, EY.

## Southern Regional Committee

On 14 October 2016, the AEB Southern Regional Committee held a round-table meeting "Experience gained in investment projects" at the Nestle Kuban factory.
Eric Heusler, CEO, LLC Nestle Kuban, Ralf Bendisch, CEO, OOO CLAAS, and representatives of other member companies spoke about their investment projects.
The participants were given a tour around the factory and then visited the Nestle guest house where they were welcomed with refreshments and had the chance to talk further in an informal environment.


The participants near the Nestle Kuban factory

At the meeting

On 17 October 2016, representatives of the AEB Southern Regional Committee spoke at the briefing for the delegation of Lower Saxony. The participants of the Business Mission of Lower Saxony arrived in Krasnodar to establish cooperation, develop trade relations and investment activity, and meet with the administration of the Krasnodar region and business representatives.
Oleg Zharko, Chairman of the AEB Southern Regional Committee, addressed the participants and talked about the aims and objectives of the completed and ongoing projects of the Southern Regional Committee in the Krasnodar region. Vladimir Druzhina, Chairman of the AEB Seed Committee, shared his experience in the investment project with the participants, drawing attention to bottlenecks and innovative solutions.

On 25 October 2016, the AEB Southern Regional Committee held a Round Table: "Flexible working arrangements". The event took place in the office of the Cargill company. Among the participants of the meeting were representatives of Cargill, CLAAS, Philip Morris Kuban, KWS, IKEA, and Nestle Kuban. The key topics of the discussion were methods and experience in the realisation of flexible working arrangements.


Participants of the meeting

## Taxation + Retail Trade Committees

On 20 October 2016, the AEB Taxation and Retail Trade Committees held a business breakfast meeting: "Trade Law Amendments: Practical Aspects". The event highlighted recent changes in trade law, including new law limitations, ban on reimbursements, and relevant practice developments. It provided an excellent platform for discussion and exchange of knowledge by professionals. Anna Likholit, Metro Cash and Carry, Pavel Gromov, Auchan, Natalya Kozlova, PwC, Nikolay Voznesensky, Goltsblat BLP, Oksana Zhupina, Deloitte, shared their expertise and gave advice on important tax and legal matters connected with trade law. The event was moderated by Alina Lavrentieva, Chairperson of the AEB Taxation Committee, PwC, and Alexey Grigoriev, Chairman of the AEB Retail Trade Committee, Metro AG.

**Alina Lavrentieva**, Chairperson of the AEB Taxation Committee, PwC, delivering a welcoming speech; **Alexey Grigoriev**, Chairman of the AEB Retail Trade Committee, METRO AG.

## Working Group on Modernisation & Innovations

On 27 October 2016, the AEB held a session on "Technological Aspects of Joining the Asian Super Ring" at the Forum Open Innovations. The session was organised by the Working Group on Modernisation & Innovations and was moderated by Michael Akim, Chairman of the Working Group, Vice President, ABB Russia.

The AEB was also represented by Philippe Pegorier, Member of the AEB Board, President, Alstom Russia. Other speakers were Elena Gorchakova, Executive Assistant of the Minister, Ministry for the Development of the Russian Far East, Bo Nilsson, Head of Sales Middle East Africa, ABB AB, Sweden, Alexander Sergeev, En+ Group, and Alexey Ponomarev, Vice President for strategy and relations with industry, Skolteh. The session aimed to discuss and analyse the steps necessary for implementing the energy ring project, connecting Russia, China, South Korea and Japan, which was recently proposed by Russian President, Vladimir Putin.

The Moscow International Forum for Innovative Development, "Open innovations", is the annual forum dedicated to new technologies and prospects for international cooperation in the field of innovation. It aims to provide an opportunity for the exchange of practical experience, the promotion of leading research studies and development projects, and the creation of new mechanisms for international cooperation in the field of innovation. It has been held in Moscow under the auspices of the Russian Government since 2012. This year, the Forum took place in Skolkovo Technopark. On 26–28 October 2016, it will host more than 90 various events organised in an interactive format: from panel discussions, presentations and lectures to workshops, pitch sessions and hackathons.

Panel session

# MEMBER NEWS

**Dear members, please be informed that you can upload your news or press releases on our website in "Member News" section via personal page absolutely free of charge.**

## Alinga Consulting

On 6 October 2016, Chet Bowling, Managing Partner, Alinga Consulting, received the Writ of Commission as Honorary Consul of Jamaica to the Russian Federation. The ceremony took place in the Embassy of Jamaica in Berlin. The Writ of Commission was signed by Mrs. Kamina Johnson Smith, the Minister of the Foreign Affairs and Foreign Trade of Jamaica.

Apart from the issue of visas and representation of the interests of Jamaican citizens, Chet will be responsible for the promotion of business between Russia and Jamaica.

**Ms. Kiesha Kal Witter**, Counsellor, and **Mr. Chet Bowling**.

## AutoPartners

Auto Partners is celebrating its 10th anniversary in Russia this year. Established in 2006, the company is a subsidiary of Credit Europe Bank Russia which owned by FIBA Group that has been active locally since 1997.

Today the company holds a position among the three largest operational leasing companies with 11% of the market share in Russia. Having it's headquarter in Moscow, the company has 13 branches which cover an area from Kaliningrad to Vladivostok. Vehicles under management are servicing in over 150 cities of Russia. The company works with 700 high quality suppliers.

Auto Partners is also the Russian partner of Athlon Car Lease which provides operational leasing services in 22 countries for more than 800,000 vehicles. Athlon is currently the 4th largest operational leasing company in Europe and has been acquired by Mercedes-Benz Financial Services in June 2016.

Auto Partners is targeting significant growth and enlarging client's number that are looking to decrease their fleet costs. For this purpose, the company will continue investing in its management systems to reach the highest level service quality and customer satisfaction with tailored fleet solutions.

## VEGAS LEX

### VEGAS LEX in IFLR1000 2017 Financial and Corporate guide

The IFLR1000 2017 Financial and Corporate rankings were published on 14 October 2016. According to the ranking VEGAS LEX* has improved and retained its prior positions in Financial and Corporate category**.

VEGAS LEX was promoted in the Project finance and Mergers and acquisitions categories and, as before, retained its positions in Restructuring and insolvency and Banking.

Chairman of the Board of Partners Albert Eganyan was noted as a leading lawyer in the Project finance category***.

In June 2016, VEGAS LEX was also recommended in Energy and infrastructure in the Energy and Mining subcategories.

***

* VEGAS LEX's expertise has been recognised by IFLR1000 guide to the world's leading financial and corporate law firms since 2010, when the firm first applied for the ranking.

** The IFLR1000 Financial and Corporate guide includes six ranking categories: Project finance, M&A, Restructuring and insolvency, Banking, Capital markets: Debt, Capital markets: Equity.

*** Albert Eganyan was noted as a leading expert:

• in the following practice areas: Energy and Infrastructure, PPP and Private Financial Initiative; and

• in the following industries: energy, transport, mining, housing and utilities, natural resources, oil and gas, and social infrastructure.

# APPOINTMENTS

## Antal Russia

### Konstantin Bryauzov is appointed as Antal Russia partner

3 October 2016, Konstantin Bryauzov joined Antal Russia as a partner. He will head the Industrial department, which includes the following practices: Natural Resources, Manufacturing, Logistics, Automotive, Agriculture, Sales of Raw Materials and Equipment, Engineering and IT.

Konstantin successfully works in HR services market since 2003, having started his career as a business development manager at Kelly Services. Later Konstantin was a Head of Adecco company for several years. In 2009, he founded Persona Citus recruitment agency, specialising in recruitment for the industrial companies in the regions. Prior to joining Antal Russia, Konstantin held the position of Director of sales at Beagle recruiting company.

"I'm glad that Konstantin, an expert with 13 years of experience in recruitment, has joined our team and will take an active part in the further development of the company. Antal Russia's industrial practice has always been one of the most powerful and important. Konstantin's experience and expertise will help us bring it to a new level," – says Michael Germershausen, Antal Russia Managing Director.

# NEW MEMBERS

## ABBYY LS

ABBYY Language Solutions is a global language technology partner and service provider. More than 2,500 companies worldwide, including 25 companies in the TOP 100 Global Brands and 35 Fortune 500 companies, rely on us for translation and localisation to deliver their businesses to the global market. We focus on translation services of any kind, workflow automation, and cutting-edge linguistic solutions to streamline multilingual content maintenance for our clients. The offering for the translation automation includes the cloud-based translation platform SmartCAT, cloud-based terminology management solution, machine translation technologies and enterprise- or domain-specific MT engines and much more. The company's advanced technological background is ensured by being a part of ABBYY Group – a leading global software developer and provider of optical character recognition, document capture, and language and translation services. ABBYY LS offers comprehensive language support to more than 2,500 corporate clients worldwide.

**www.abbyy-ls.com**

## Andrey Gorodissky and Partners Law Firm (AG&P)

Andrey Gorodissky & Partners was founded in 1992 and is recognised as one of the leading Russian law firms of business lawyers. The firm is highly specialised in the provision of comprehensive services to foreign companies and financial institutions doing business in Russia. The firm has a global client base, and its partners have the status of advocates under Russian law. The firm has unparalleled experience in handling complicated cross-border transactions and investment projects involving participants and counsel located in various jurisdictions. The lawyers of the firm have in-depth knowledge of Russian law and the practice of its application, as well as a profound understanding of the country's economic, political and social environment, combined with a good command of western standards and rules of doing business. AGP lawyers have full legal knowledge relevant to such industries as smelting, automobile manufacturing, IT, construction, medical, food, trade, and consumer goods.

**www.agp.ru**

## Covestro

With 2015 sales of EUR 12.1 billion, Covestro is among the world's largest polymer companies. Business activities are focused on the manufacture of high-tech polymer materials and the development of innovative solutions for products used in many areas of daily life. The main segments served are the automotive, electrical and electronics, construction and sports and leisure industries. The Covestro group has 30 production sites around the globe and employed approximately 15,800 people at the end of 2015. Covestro is a Bayer Group company.

**www.covestro.ru**

## Ericsson

Ericsson is the driving force behind the Networked Society – a world leader in communications technology and services. Our long-term relationships with every major telecom operator in the world allow people, business and society to fulfill their potential and create a more sustainable future. Our services, software and infrastructure – especially in mobility, broadband and the cloud – are enabling the telecom industry and other sectors to do better business, increase efficiency, improve the user experience and capture new opportunities. With approximately 115,000 professionals and customers in 180 countries, we combine global scale with technology and services leadership. We support networks that connect more than 2.5 billion subscribers. Forty percent of the world's mobile traffic is carried over Ericsson networks. And our investments in research and development ensure that our solutions – and our customers – stay in front.Founded in 1876, Ericsson has its headquarters in Stockholm, Sweden. Net sales in 2015 were SEK 246.9 billion (USD 29.4 billion). Ericsson is listed on NASDAQ OMX stock exchange in Stockholm and the NASDAQ in New York.

**www.ericsson.com**

## European Consulting Group

The idea behind the creation of the company was to provide a service enabling an individual to feel completely safe in terms of legal security regardless of what he or she is doing or where he or she is. Unlike many other lawyers, we are not bound by traditions. Yes, we like order in everything, but we are distinguished by innovative thinking. Every day we are looking for ways to become more efficient, following the development of technologies and implementing them to improve our service. For the long term, we see all our clients having a map/application allowing to obtain any help in any part of the world, whether it is booking of tickets, office rent, legal or accounting advice, registration of a new company or translation of an article to a required language. We work both with big companies and individuals. Our clients are everywhere that is why we are growing so rapidly. Our offices are located in Russia, Hong Kong, China and Slovakia. We are working to provide absolute care to our clients. Summary of our services: legal services; accounting services; business references; real estate services; appraisal services; consultations.

**www.e-c-g.ru**

## EUROMONT LLC

OOO "EUROMONT" is an Austrian company, which provides services on installation of mechanical equipment, metal constructions, ventilation and aspiration systems, pneumatic pipelines, services on electric installation, repair and maintenance for industrial equipment and many others. Our team consists of highly qualified engineers and designers, experienced specialists in the sphere of montage, welding works and electrician installation. EUROMONT works geography covering both the territory of the Russian Federation and CIS Countries. The long-term practice and experience in the sphere of industrial installation and design, as well as impeccable observance of customer`s requirements and terms of works execution remain our strongest points. Working with small and large enterprises, EUROMONT continues to successfully solve any task connected with equipment installation and optimisation.

**www.euro-mont.eu**

## Faiveley Transport

Faiveley Transport is a global supplier of high added value integrated systems for the railway industry. With almost 6,000 employees in 24 countries, Faiveley Transport generated sales of €1,105 million over the 2015/2016 financial year. The Group supplies manufacturers, operators and railway maintenance bodies worldwide with the most comprehensive range of systems on the market: Energy & Comfort (air conditioning, power collectors and converters, and passenger information), Access & Mobility (passenger access systems and platform screen doors), Brakes & Safety (braking systems and couplers) and Services.

**www.faiveleytransport.com**

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## Fidia Farmaceutici

Fidia Farmaceutici is a privately held, fully integrated Italian pharmaceutical company, with R&D, manufacturing, marketing, and sales capabilities. The company was founded in Bologna (Italy) in 1946 and relocated to Abano Terme (Italy) in 1959, is part of the P & R Group since 1999, ranked among the top ten national chemical groups. It counts more than 1,800 employees (increased by 22% in 3 years), distributed between the chemical and pharmaceutical market segments. Fidia Farmaceutici and its associated companies operate worldwide with the aim of developing and marketing innovative healthcare products (medicinal products, medical devices, and dietary supplements), primarily based on proprietary hyaluronic acid (HA) and its derivatives. More than fifty years of research into this molecule have placed Fidia at the forefront in the production of both natural and functionalised hyaluronic acid, utilising proprietary and validated extraction and biotechnological processes. Fidia is continually working to identify new opportunities and holds an extensive patent portfolio worldwide covering HA molecular weight fractions, industrial processes, pharmaceutical formulation/composition, derivatives, and uses. Fidia's know how of hyaluronic acid has enabled the company to develop Innovative, integrated solutions (hyaluronic acid-based viscosupplementation) for the management of joint diseases, among them Hyalgan for the intraarticular therapy of osteoarthritis.

**www.fidiapharma.com**

## Flex

More than 12 years the Company specialises in searching and staff recruitment.Our Company provides the following kind of services for the employers: recruitment of the beginning, middle and top management teams; regional recruitment in Russia and CIS (Ukraine, Kazakhstan, Belarus). For job seekers the agency provides the following free of charge services: consulting on current labour market tendencies; searching of the interesting and perspective positions of our Clients; interview training; candidate support till the moment of placement during the probation period. We specialise in recruitment in the following business areas: medicine, pharmaceutics; FMCG; banks, investments, financial consulting; legal consulting; IT & telecommunications; and sectors: top-management; sales; PR, marketing, advertising; procurement, logistics; finance, accounting; law; administrative staff; IT, telecommucations; HR; installations & services.

**www.flexsearch.ru**

## FM Logistic

FM Logistic is one of the leaders on the Russian logistics market. The company offers the whole range of supply chain management services, such as storage, carriage by all types of transport, co-packing and co-manufacturing, customs clearance.

**www.fmlogistic.ru**

## Gosselin Mobility Moscow

Gosselin Mobility is a well-known European relocation company serving the customers through 48 offices in 32 countries throughout Europe, Russia, the Caucasus and Central Asia and a global network of moving partners. Gosselin provides worldwide relocation and moving services for domestic, long distance and international moves. The company offers a comprehensive range of pre-departure services, including orientation tours and welcome packs, designed to ease the assignee and their family into their new location. From transporting belongings to the new location, to help finding a new home, to connecting utilities, to doing it all in reverse on the way back home, Gosselin Mobility takes care of absolutely everything. Over and above a comprehensive range of relocations services, the company also provides consultancy services to cater for the increasing diversity and complexity of international assignments. Move management services, visa & immigration services, corporate policy design, global expense management, compensation administration and more, you can trust Gosselin to masterfully take care of even the trickiest of international relocations. With over 50 years' experience relocating expats and their families around the world, Gosselin is an absolute expert in making the transition to a home away from home as smooth as possible.

**www.gosselingroup.eu**

## IKEA Centres Russia

IKEA Centres Russia, part of the IKEA Group, owns, develops and manages a chain of major shopping centres throughout Russia. It provides circa 2 million $m^2$ of retail space, and more than half its tenants are represented by international retailers. Each mall typically comprises around 130,000 $m^2$ with about 200 retailers and each MEGA centre benefits from an IKEA store as a powerful anchor, together with a food hypermarket and DIY store. MEGA enjoys 95% brand recognition in Russia, and it is the first name that comes to mind when consumers wish to go shopping.

**www.ikea.ru, www.ikeascr.com**

## ITAMAA

Itamaa is a specialised service provider in accounting, company administration and sales representation in Russia. Our clients are local and International small and medium-sized companies from several branches of industry. Our experienced English-speaking accounting and reporting specialists together with the latest accounting software enable a cost efficient and risk-free accounting and administration service in the Russian market.

**www.itamaa.fi**

## Mercuri International

Mercuri International is a global organisation that is comprised of over 450 full-time highly experienced sales and leadership professionals in over 50 countries that have helped over 15,000 companies worldwide optimise their sales results. Methodologies are supported through continuous development and refinement in St. Gallens University; with programmes ranging from Sales Productivity Planning, Selling Skills, Complex Consultative Value Selling, Leadership Development and Coaching Skills, Blended Training utilising state of art e-learning, and Client Specific Business Games. Industry areas of expertise include: FMCG, Technology, Finance, Medical, Pharmaceutical, Manufacturing, Electronic Security, and numerous others.

**www.mercuri.net**

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