



ProsperoScope

Prospects, comments, solutions

Introduction

The Federal Portal of Draft Regulatory Acts has published a Draft Federal Law¹ (hereinafter referred to as **the Draft Law**) that includes a number of long-awaited amendments to the taxation rules on controlled foreign companies (CFCs). Among these are changes in rules for taxation of CFC's profits and tax-free CFC liquidation benefit.

In this edition of ProsperoScope, we'll highlight the most relevant aspects of these amendments for private clients.

A complete analysis of the Draft Law will be issued after its review by the Russian State Duma.

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Proposed amendments on the voluntary disclosure by individuals of assets and bank accounts²

As publicly announced by the Ministry of Finance, these amendments should extend the terms of the voluntary declaration campaign as well as expand the list of assets to be declared. The promise is to free individuals from repatriating shares of offshore companies and allow them submitting information of property sold in the special disclosure forms to tax authorities, which is currently not allowed.

Proposed amendments to the CFC legislation

Procedures and terms for submitting notifications of participation in foreign companies (establishing foreign structures without forming a legal entity)

- Individuals controlling foreign structures or having the actual right to income generated by them will be exempt from the obligation to submit participation notifications. This implies that only setters of foreign structures will have to submit participation notifications – not beneficiaries or other persons.
- If an individual is acknowledged as a controlling person in a non-incorporated foreign organization (or any other legal entity having no capital or fund), this participation shall also be taken into consideration when defining the participation share in the foreign organization.
- The current Russian Tax Code does not stipulate any procedure for submitting participation notifications in cases where an individual who was not a Russian tax resident as of the date of his or her participation in the foreign company becomes one by the end of the relevant calendar year. The Draft Law specifies that in such a case, the participation notification shall be submitted on or before 1 February of the year following the indicated calendar year.

In this regard, the participation interest as well as the fact of availability of the company for the purpose of notification is determined at 31 December of the said calendar year.

Considering the above the requirements for submission of the notifications become clearer.

Procedure for calculating taxable income of a CFC

- A CFC's income can be calculated based on its financial statements if one of the following criteria is met:
 - The CFC permanently resides in a foreign state that has a Double Tax Treaty with Russia in place, except for states not exchanging tax information with Russia (see details in our [ProsperoScope of 9 November 2015](#));
 - An audit report for the relevant financial period contains no negative opinion or a note that the possibility to express an opinion was declined.

The amendments will also allow for the results of either mandatory or voluntary audits of the relevant statements to be used for calculating CFC income, simplifying the process in many cases (versus the calculation based on the Russian Tax Code).

- Income of a taxpayer that is a controlled entity in the form of dividends obtained upon distribution of CFC income shall be exempt from taxation if this income has been included into the personal tax return (3-NDFL) and documents confirming this are in place. This eliminates the existing issue of double taxation of the income of a taxpayer that is a controlled entity.

Tax-free liquidation of a foreign organization (cessation of a foreign structure)

- Benefits resulting from the tax-free liquidation of a foreign organization (cessation of foreign structures without a legal personality) will be extended until 1 January 2018. Additionally, if the decision to liquidate a CFC is made prior to 1 January 2017, but the procedure cannot be completed until 1 January 2018 due to the limitations imposed by the CFC governing law or because the CFC is involved in a lawsuit, provisions on the tax-free liquidation shall apply until the end of such limitations or litigation.

- An individual who is a controlling person shall not derive income in the form of a deemed income when purchasing securities from a CFC at the documented value of these securities in the CFC's books if the decision to liquidate the CFC has been made or initiated on or prior to 1 January 2018 – or even later in some cases. In case of a further re-sale of these securities, the income can be decreased by actual expenses defined as the cost of these securities at the date of the securities ownership transfer, but not exceeding the market value at this date. This allows additional opportunities for business restructuring.

It is worth noting that the Draft Law may be amended significantly by the time it is submitted to the State Duma, or during hearings in the Duma. We will keep you updated!

¹The Draft Federal Law "On amending parts one and two of the Russian Tax Code and the Federal Law of 24 November 2014 'On amending parts one and two of the Russian Tax Code (regarding taxation of the income of controlled foreign companies and the income of foreign organizations).

²The Federal Law No 140-FZ of 8 June 2015 "On voluntary declaration of assets and bank accounts (deposits) by individuals and on amendments to certain legislative acts of the Russian Federation."

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Contacts

We hope you find this information useful and interesting. If you have any questions, please feel free to contact us.

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