

Legislative Tracking



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29 July 2016

E-justice: catalogue of commercial cases

http://kad.arbitr.ru/PdfDocument/363141a1-547c-460f-b4c5-aba8d3b5a45f/A40-81712-2015_20160719_Reshenija%20i%20postanovlenija.pdf

Court recognises share repurchases from foreign parent as indication of concealed distribution of dividends

The Commercial Court of the City of Moscow Decision of 19 July 2016 on Case No. A40-81712/2015 has been published. The case concerned the tax authorities' challenge of the deduction of interest on a loan from a Russian company affiliated with a foreign parent by applying the thin capitalisation rules and levying withholding tax on the interest paid to the Russian lender, as the tax authorities considered a share buyback performed by said Russian company to be a concealed distribution of dividends.

The court of the first instance and the appellate court ruled in favour of the tax authorities, while the court of cassation referred the case for retrial, calling for an investigation into the episode involving the assessment of the withholding tax liabilities (taking into account the affirmative Russian Supreme Court Ruling of 18 March 2016 on a similar case).

During the retrial proceedings, the Commercial Court ruled in favour of the tax authorities, referring to the circumstances indicative of the subsequent distribution of the funds by the Russian affiliate in favour of the parent by repurchasing its shares from the foreign company.

The court highlighted the specificity of the financing arrangements between the parent registered in Cyprus, the Russian lender (Megapolis Trading Company) and the Russian borrower (NTK), both affiliates of the former:

- Megapolis Trading Company wished to increase its registered capital by issuing additional shares; all of these shares were purchased by the foreign parent and paid for through the transfer of a 90-percent stake in the borrower's equity;
- Megapolis Trading Company extended a loan to the parent;
- Megapolis Trading Company subsequently wished to reduce its registered capital by repurchasing its shares from the parent; the amount of the repurchasing transaction was offset against the parent's debt on the loans received from Megapolis Trading Company (as a result, Megapolis Trading Company avoided returning 85 percent of the funds previously transferred to Cyprus from the Russian Federation).

The court found these circumstances to be indicative of the fact that the purpose of the coordinated actions undertaken by the company and its affiliates was the concealed distribution of dividends in favour of the foreign parent.

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