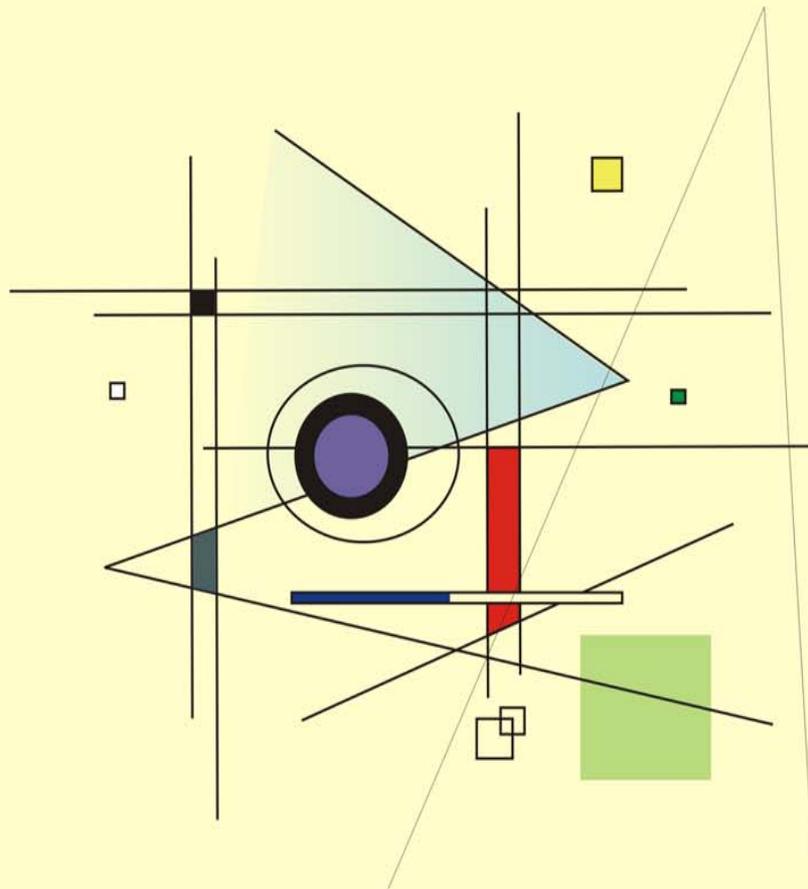


# ДМИТРИЯ ЛАБИНА

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# Double Taxation and Recent Changes in Tax Regime

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# Current Cyprus – Russia DT Regulation in Force



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- **Key Legal Instrument:** *Agreement between the Government of the Republic of Cyprus and the Government of the Russian Federation for the avoidance of double taxation with respect to taxes on income and capital as of 05/12/1998 (hereinafter – Agreement 1998).*
  
- The Agreement 1998 is generally based upon the OECD Model with a few deviations.
  
- **Scope of the Agreement:**
  - ✓ elimination of double taxation (DT) on income and capital;
  - ✓ national treatment in tax matters;
  - ✓ legal basis for exchange of information (EOI) (yet not in effective operation);
  - ✓ legal basis for assistance in collection of taxes (yet not in effective operation).
  
- **Key principles of DT elimination:**
  1. In default – *residential principle*.
  2. Interest and royalties – *principle of money inflow*.
  3. Dividends – *residential principle, limitation of the rate principle*;
  4. Real estate – *lex rei sitae*: the possibility of the state of real estate location to impose tax both on the estate itself and on transactions concerning the real estate.
  5. The method of DT elimination – *Set-off Method*: the sum of the foreign tax shall be deducted from the tax obligation of the state.

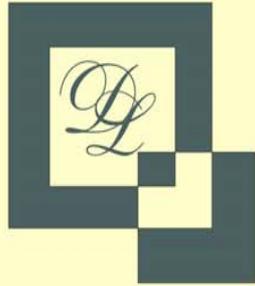
# Protocol to the Agreement 1998

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- The Protocol changing the Agreement 1998 was signed in 2010 and contains a few important innovations to the Agreement 1998.
- The Protocol 2010 is not yet not in force.
- **Key legal innovations to the DT Regime:**
  - Enlargement of scope of permanent establishment (Article II).
  - Taxation on real estate investment funds including trusts (Article III).
  - Taxation on sale of shares in companies with 50% of the assets thereof consists of real estate (Article VII).
  - Specification of “interest” and “dividends” definitions (Article V and Article VI).
  - Benefits limitation (Article XI).
  - Assistance in the collection of taxes (Article X).
  - Exchange of the information (Article XI).
  - Other innovations.

# Assistance in the Collection of Taxes



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- **Existing rule according to the Agreement 1998:**  
There set forth the possibility of assistance in absence of the list of means and measures thereof => yet have not been applied
  
- **Innovations via the Protocol 2010:**
  - ✓ specification of definition of “*tax obligation*”;
  - ✓ the 2 means of assistance to be enacted:
    - 1) unconditional recovery and
    - 2) unconditional injunction of tax obligations;
  - ✓ general obligation of the States to assist unless *ordre public* clause is applied and the measures requested contravene “*law and administrative practice of this or the other Contracting State*”.
  
- **Conditions to be met from the Cypriot side:**  
Article X of the Protocol imposes an Cyprus obligation to enact necessary legislation for the rule of assistance to be applied.

# Exchange of the Information. General Background.



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- Exchange of the Information Clause (EOI) was the most politically significant issue in relations between Cyprus and Russia in the sphere of DT.

Due to Cyprus agreement to enact the modifications to the existing clause Cyprus was removed the Russian “Black List”.

- The formula to be enacted is based on the Article 26 OECD Model Convention as of July, 2010. => it should be constructed through OECD legal and political position.
- OECD **political position**: “The era of banking secrecy is over”. The position was expressed within G20 Summit, London, April 2009.
- OECD **legal position** is embodied in OECD Council’s acts containing model rules and guidelines and practice of application thereof both in the field of corporate structure and in the field of taxation.

# Exchange of the Information. Key Legal Provisions.

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## Key the Protocol 2010 EOI Clause provisions :

- “Foreseeable Relevance” Standard vs. “Fishing Expeditions”: combination of wide application extent and limitation by reason of relevance to tax matters.
- Enlargement of scope: all taxes and tax obligations that do not go against the Agreement 1998.
- Special rule on lack of the State’s necessity in the requested information: no such a reason may be a legal ground for the refusal for application of EOI Clause.
- Cancellation of banking secrecy: exchange of information rule goes beyond any banking secrecy and secrecy treatment of information of any person’s property interests.

# Exchange of Information. Limitation of Application.

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## The limitation for the Protocol 2010 EOI Clause application:

- Taking EOI measures should not contravene the requested State's legislation and administrative practice.
- Information should be obtainable under the laws or in the normal course of the administration of both of Russia and Cyprus.
- *Trade Secrecy and Ordre Public Clause.*

NB: Banking secrecy as well as property interests are not treated as Trade Secrecy.

# Current Russian Legislation as for Beneficial Property Interests

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## Key legal issues for application of Para 3. of the Protocol 2010 EOI Clause:

- **General Rule:** for purposes of taxation and tax administration all institutes, definitions and terms shall be applied in the sense the relevant branch of law (Article 11 (1) of the Russian Tax Code).
- **Property interests:** the Russian Civil Code that does not establish any beneficial rights except those which compile ownership. => Russian legal system does not recognize *beneficiaries* and *trusts*.
- Russian civil legislation to have recently been under enhanced reformation:
  - The Concept for Civil Legislation Development as of 2009 (not legal binding document containing lawmaking framework in view of current judicial practice).
  - The Project for Lawmaking Initiatives in the Field of Civil Legislation as of 2010 containing direct modifications to the Russian Civil Code (highly arguable document, now is under discussion).

# Civil Legislation Reformation



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- Due to the dynamics of market relations and the necessity to develop civil regulations **The President's Council for codification and improving the civil legislation** was established in 1999.  
**Mandate:** advisory body / maintenance of cooperation between the authorities and civil society in considering issues relating to the civil legislation.  
**Decisions:** nonbinding effect, underlie the succeeding lawmaking initiatives.
- In 2008 the President Dmitry Medvedev assigns to the Council elaboration of **the Concept for Civil Legislation Development**.  
One of the pursued goals of the Concept: "*approximation provisions of the Russian Civil Code with rules for the appropriate relations in law of the European Union*".
- 07/10/2009 the Concept for Civil Legislation Development was approved by the Council and the work on lawmaking initiatives for civil legislation started.
- 13/10/2010 The Council published the succeeding modifications to the Civil Code.
- Summer 2011 The Working Group on Creation a Financial Center in Russia suggested profound correctives to the modifications previously suggested.
- Until now, the discussion of the modifications has been a hot issue for lawyers.

# Key Provisions of the Reformation



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## ■ The following are key provisions of the Concept 2009:

- The rights in corporations and other legal entities are suggested to be characterized as *corporate rights* as opposed to ownership rights for shares in the corporation that is used now. The corporate rights should include all rights both of property and obligation character (as a continental law system may recognize them). (Cap. III Sec. 1.1)
- Legal capacity of legal entities from Tax Heavens and foreign jurisdictions is suggested to appear within the territory of the Russian Federation on registration in Register of Legal Entities with compulsory disclosure of information relating to shareholders and beneficiaries. (Cap. III Sec. 1.9)  
=> recognizing of all transactions within Russia will be depends upon meeting this standard.

## ■ The key provision of the Modifications as of 2010:

Art.51(8) of the Draft Russian Civil Code:

*“A legal entity registered within the territory of a foreign state that accommodates preferential tax treatment and (or) not demanding delivering or disclosure of information upon financial transactions, may carry out entrepreneurial activity within the territory of the Russian Federation provided that it has deposited to the authorized state body for justice the valid information of its shareholders and beneficiaries. The list of such foreign states shall be defined by the authorized state body. The deposited information may be disclosed by the legal entity itself or under the court decision. Risk for depositing invalid information as well as carrying out entrepreneurial activity without depositing the mentioned information shall be born the legal entity.”*

# Putin's Proposals

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**Mr. Vladimir Putin proposed in his article as of 30/01/2012 in the newspaper “Vedomosti” the following:**

- In the context of the necessity to improve Russian business climate as one of 3 vectors for enhanced developing of Russian economy:

*“We are losing in the “competition of jurisdictions”. Enterprises functioning in Russia often prefer registration property and transactions abroad. And the reason for it is not the tax regime – it is generally competitive, and not is it the lack of legislation meeting contemporary requirements (though, sure, it needs enhancing: it is still insufficiently flexible and lacks a complete set of instruments for business)”.*

- In the context of the call for funds from private persons as one of 3 vectors for enhanced developing of Russian economy:

*“We need state projects for engagement of people’s money – though pension funds and trust funds, collective investments funds. In states of developed market economy these are a significant part of national capital”.*

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