

Newsletter

Residency issues of 2020

April 28th, 2020

Dear Ladies and Gentlemen,

This year has forced changes to the plans of many people around the world. A few months ago, it was hard to imagine that meetings and deals would be arranged only by video link, offices equipped at home, and that vacation, or a long-awaited meeting with your family, would depend on the measures of a particular state to prevent the spread of the virus and policies to close borders. This new way of private and business life may lead to new realities of taxation, residency and application of currency legislation.

It is already clear that earlier strategies for living in certain countries, making investments, performing different types of transactions and taxation of certain types of income may not work, due to the forced stay in a country different from the country of your "ordinary", or intended residence.

Despite the fact that, in certain cases, the provisions of the Double Taxation Agreements may still be applicable, and states may adopt special tax-residency rules for the year 2020, individuals may nevertheless face new requirements that apply to them in the country of their actual residence, for the current year.

The above-mentioned refers in particular to the following groups of individuals:

- (A) Those, who mainly live outside the Russian Federation and are subject to taxation under foreign law, but due to the pandemic situation, will spend more than 183 days in Russia in a calendar year, ended 31st December 2020;
- (B) Those, who currently stuck outside the Russian territory, but normally live in Russia and are Russian tax residents.

The change of tax status may lead to a number of legal consequences, both for the individual and for his/her business in Russia and abroad.

In addition, the number of days spent on the territory of the Russian Federation affects not only taxes, but also obligations (and in some cases restrictions) under the Russian currency legislation.

ALRUD team has prepared guidance material for better understanding of the specifics of Russian tax and currency resident status:

Currency control issues for special residents 2020

Tax issues for individuals, Russian tax residents 2020

The tax issues for individuals, who are non-residents in the Russian Federation, but receive income from Russian sources, should be analyzed separately. If, due to the current situation in 2020, a non-resident individual is not able to obtain a Tax Residency Certificate in the "usual" jurisdiction (e.g. due to a long stay outside the "usual" jurisdiction), the following is recommended:

- To check the criteria for tax residency in the country (countries) of stay in 2020, analyze possible consequences of being recognized as a tax resident in that jurisdiction (those jurisdictions);
- To check the applicable Double Taxation Agreement between that jurisdiction (those jurisdictions) and the Russian Federation, if income from Russian sources is received;
- To contact the tax authority of the "usual" country of residence to clarify the possibility of obtaining a Tax Residency Certificate for 2020, taking into account the current situation.

Russian currency control issues concerning residents, who lose the status of “special” resident in 2020

In accordance with the currency legislation, all citizens of the Russian Federation, as well as foreign citizens and stateless persons permanently residing in the Russian Federation on the basis of a residence permit, are considered currency residents.

Residents who stay outside the Russian Federation during the calendar year, for more than 183 days, have a “special” status and the exemption right to submit notifications on foreign accounts, reports on the movement of funds over the accounts, and most of the restrictions on currency transactions.

For residents who previously mainly lived abroad, but whose period of stay in the Russian Federation in 2020 will exceed 183 days, the following should be noted.

Currency transactions performance in accordance with currency legislation

Changes to the currency legislation, at the end of 2019, significantly expanded the list of permitted currency transactions on bank accounts opened in the most popular jurisdictions.

Nevertheless, when the currency status is changed, it is advisable to check the operations, usually performed on foreign accounts, for their compliance with the Russian currency legislation.

In particular, the following issues should be noted and analyzed:

- loss of the right to conduct direct transactions between foreign accounts of “special” residents;
- jurisdictions, in which bank accounts are opened. These [changes](#), adopted in 2019, establish a different regime for bank accounts opened in the countries:
 - performing the automatic exchange of information with Russia under CRS and
 - not performing such exchange of information.

For example, the United States, Canada and the United Kingdom fall into the second group and, therefore, operations on bank accounts located in these countries are significantly limited.

Thus, it is forbidden to credit income from portfolio investments to accounts opened in these countries (including cases where investment is made for visa purposes), from renting out property, and in many other cases.

Foreign accounts reporting obligations

If the status of the “special” resident is lost in 2020, there will be an obligation to submit the following documents regarding the accounts opened with banks, or other financial market organizations, located outside the Russian Federation:

- Notification on opening/closing/change of bank details:
 - Before the 1st of June 2021 – in respect of the accounts opened prior to 2020;
 - within one month from the date of opening of the account – in respect of the accounts opened in 2020.
- Report on foreign accounts transaction movements for the year 2020 – before the 1st of June 2021.

In this respect, it is recommended to:

- Consider the possibility to change usage of bank accounts in jurisdictions that do not automatically exchange information with the Russian Federation and, if possible, redistribute cash flows in order to prevent violations of the currency legislation;
- Ask the bank, or other financial market organization, to inform immediately about opening new accounts, closing existing ones, or changing their details;
- Check with a foreign bank, or other financial market organization, whether the tax status in the bank’s internal systems will be adjusted under current conditions for CRS purposes.
- After the end of 2020, request from the banks, and other organizations of the financial market, statements of accounts for the calendar year to arrange timely preparation of the currency reporting documents, as described above.

Repatriation

This is to remind that Russian currency residents (regardless of the status of the “special” resident) are required to ensure that the funds, granted under loan agreements, are received from non-residents in their accounts with Russian banks, within the terms provided for by such agreements.

Tax issues for individuals who will become Russian tax residents in the year 2020

Tax residency

Individuals, who spend more than 183 calendar days during 12 consecutive months, in the Russian Federation, are considered to be Russian tax residents. The final tax status of a person is determined for a calendar year.

Those who will spend more than 183 calendar days in the Russian territory in 2020 (further the "Residents") should note the following issues, which may affect their tax liabilities:

- Controlled foreign company (CFC) rules;
- Possibility to recognize a foreign company as a Russian corporate tax resident;
- Taxation of incomes received from Russian and foreign sources.

Additional issues

On March 25th 2020 the President of the Russian Federation announced the introduction of 15% tax on dividends and interest payable abroad from Russia and an upcoming revision of the Double Taxation Agreements ("DTA") with 'transit' (offshore) jurisdictions. These changes may have a negative effect on the taxation of cash flows within foreign holding / financial structures that own Russian companies, or provide them with financing. Based on public information, the Russian authorities has already sent official requests for changes of DTAs to Cyprus, Malta and Luxembourg.

More detailed information on obligations of individuals, who will become Russian tax residents in 2020, is presented below.

Controlled Foreign Companies (CFC)

A foreign company is treated as a CFC in case the Resident:

- owns more than 25% of the company, or
- owns more than 10% together with spouse and minor children, if the participation share of all residents of the Russian Federation in the company exceeds 50%, or
- exercises control over the company in his/her personal interests, or in the interests of his/her spouse and minor children.

Foreign structure without legal entity (further the «Structure»), including trusts, foundations, partnerships and others, is recognized as a CFC, when the Resident:

- is its founder (with some exceptions), or
- is not its founder, but exercises control over the Structure and also meets one of the following conditions:
 - the Resident has the actual right to receive income from the Structure (or part of income), or
 - the Resident has the right to dispose of property of the Structure, or
 - the Resident has the right to receive the property of the Structure in the event of its termination (liquidation, or termination of the agreement).

Foreign companies and structures

Reporting and tax obligations according to CFC rules

Disclosure obligations for Residents – controlling persons of CFC

Residents are obliged to submit the following documents to the Russian tax authorities:

- (A) Notification of participation in a foreign legal entity, or establishment of structure:
- Before the 1st of March 2021 – if the participation began prior to Resident status acquisition and Notifications were not submitted previously,
 - within 3 months from the date of participation (establishment) – if the participation began after Resident status acquisition.
- (B) CFC Notification for the period 2020 (in respect of the 2019 financial year of CFC) – before 20th of March 2021.

CFC profit calculation and declaration

If the profit of a CFC for 2019 financial year exceeds 10 mln. Russian Roubles, the following additional obligations of Resident arise:

- (C) To include the profit of the CFC in the tax declaration, which should be submitted together with the financial statements of CFC (and auditors report, if applicable) before 30th of April 2021,
- (D) To pay tax on the profit of the CFC, at the tax rate of 13%, before 15th of July 2021.

Practical recommendations

- To analyze the ownership structure of foreign companies, trusts, foundations, as well as participation in partnerships and determine the scope of companies and Structures that fall under the definition of CFCs and, for which, disclosure is required,
- To identify companies and Structures which generated taxable profits exceeding 10 million rubles for 2019, and to organize the preparation of financial statements and their audit (if applicable),
- To identify the existence of grounds for exemption of CFC profits from taxation (e.g. possibility to qualify it as an “active” company and other),
- To prepare documents confirming absence of an obligation to submit CFC reports for previous periods (copies of foreign passports, tax residency certificates of foreign states and other).

Recognition of a foreign company as Russian tax resident

A foreign company may be treated as a Russian tax resident if a Resident or, another individual permanently staying in the territory of the Russian Federation, holds a managing position and/or exercises actual management of such foreign company from the territory of the Russian Federation.

Consequences: Russian income tax (20%) is applicable to the entire worldwide income of the foreign company, irrespective of the place(s) where it is earned.

Important!

Recognition of a foreign company as a Russian tax resident excludes its qualification as CFC.

Practical recommendations

- To analyze the current management structure of foreign companies and estimate the possible tax consequences,
- To make changes in the management structure of foreign companies (if applicable).

Taxation of Resident's incomes

Income from the sources outside the Russian Federation

All of the worldwide income of a Russian tax resident is taxable in Russia.

In this regard, some income, not previously taxed in the Russian Federation, will be subject to inclusion in the tax base of those persons who will acquire the status of tax resident in 2020 (e.g., such income will include rental payments received in other countries, income from investment portfolios held outside Russia and other).

Particular issues of the Russian taxation:

- The applicable tax rate (13%) is one of the lowest in Europe,
- Income and expenses received (paid) in foreign currency must be converted into Russian Roubles, at the exchange rate of the Central Bank of the Russian Federation, at the date of their actual receipt/payment. This may cause taxable income in the form of exchange differences,
- If there is applicable DTA, it is possible to offset tax paid abroad against the Russian tax. Since the tax rate in many jurisdictions (for example, Switzerland, Germany) exceeds 13%, the tax payable in the Russian Federation may not arise. However, this does not extinguish the obligation, to declare income and provide documents confirming payment of the foreign tax.

Practical recommendations

- To estimate the amount of taxable income in the Russian Federation,
- To revise portfolio management strategy, taking into account the items below:
 - Scope of transactions, which should be declared (each transaction is included in the tax return separately, which creates a significant volume of administrative work in the case of a large number of transactions),
 - potential taxable income in the form of Rouble exchange differences arising for sale (redemption) of securities,
- To start gathering confirmation documents regarding payment of tax abroad in advance (if applicable).

Planned transactions for the sale of shares, stocks, real estate, etc.

If any large transactions are planned for the year 2020, it should be noted that income from such transactions would be taxed in the Russian Federation at the rate of 13%.

At the same time, certain types of income may be exempt from taxation. For example, income from the sale, or redemption, of participating shares in the authorized capital of Russian organizations, as well as from sale of certain Russian shares, is not taxed, provided that, on the date of the sale (redemption) of such participation shares (shares), they had been continuously owned by the taxpayer for more than 5 years.

Practical recommendations

- To analyze transactions planned for the year 2020 and estimate the tax consequences,
- To prepare supporting documents for exemption of revenues from taxation, or for deduction of expenses related to acquisition of the assets sold.

Please keep yourselves safe! We will be working for you and keep you posted on the relevant legal developments.

For up-to-date legislative news and business-related guidance in connection with COVID-19, please visit our dedicated webpage:

COVID-19: What you need to know

We hope that the information provided herein will be useful for you. If any of your colleagues would also like to receive our newsletters, please send them the link to complete a [Subscription Form](#). If you would like to learn more about our [Tax Practice](#), please let us know in reply to this email. We will be glad to provide you with our materials.

Note: Please be aware that all information provided in this letter was taken from open sources. Neither ALRUD Law Firm, nor the author of this letter, bear any liability for consequences of any decisions made in reliance upon this information.

We will be glad to answer your questions!



**Maxim
Alekseyev**
Senior Partner
Tax

E: malekseyev@alrud.com



**Elena
Novikova**
Of Counsel
Tax

E: enovikova@alrud.com

Sincerely,
ALRUD Law Firm