



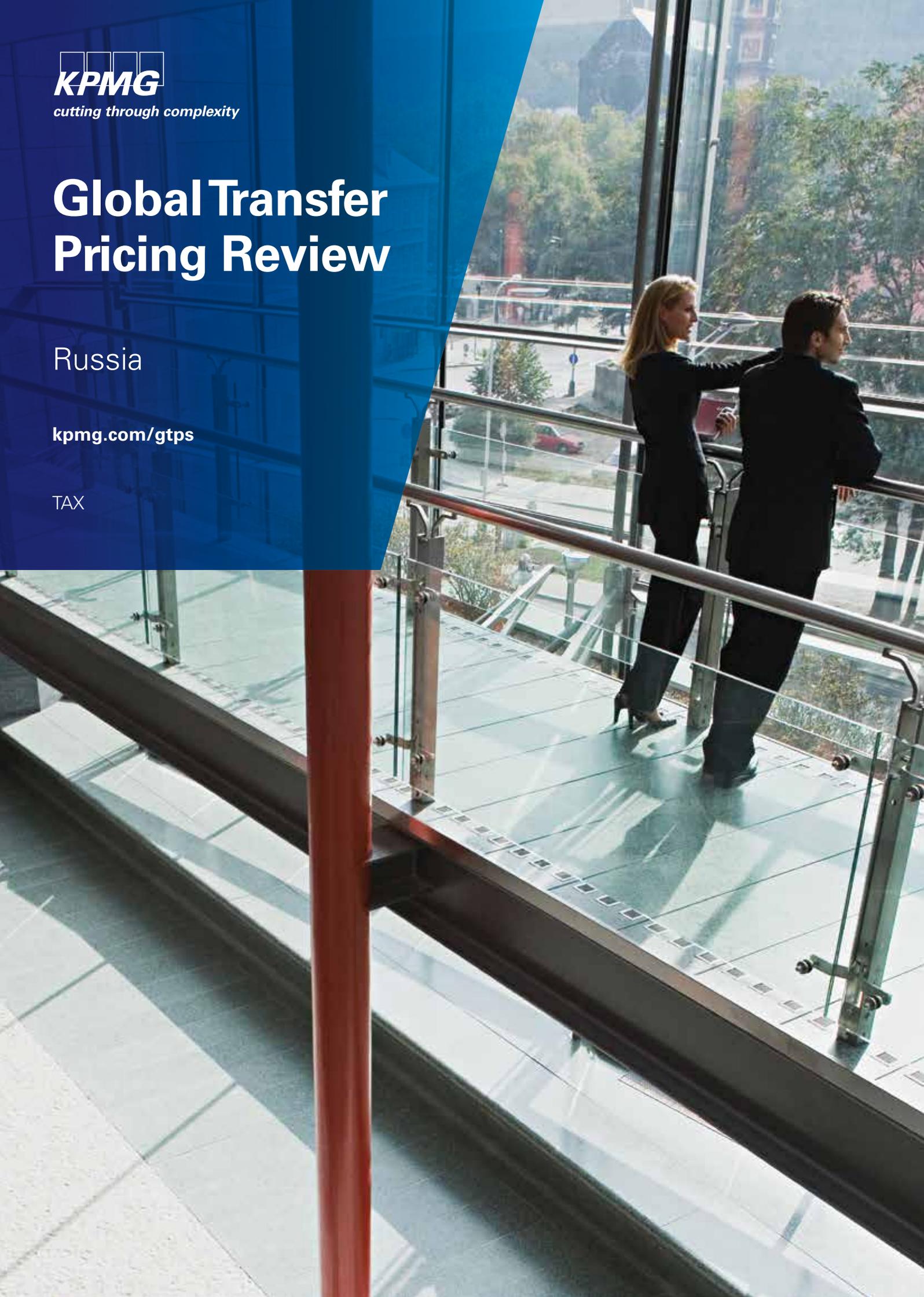
cutting through complexity

Global Transfer Pricing Review

Russia

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TAX



Russia

KPMG observation

The current Russian transfer pricing rules have been effective since 2012. They are generally based on the Organisation for Economic Co-operation and Development (OECD) Guidelines, but have certain differences. For example, while there are five basic transfer pricing methods (as in the OECD Guidelines), under the Russian transfer pricing rules, the Comparable Uncontrolled Price (CUP) method and Resale Price Method have priority over other methods.

Under Russian law, even large domestic transactions between related parties are subject to the transfer pricing rules. Furthermore, the Russian tax authorities may control prices not only in cross-border transactions with related parties, but also in transactions with unrelated companies located in offshore jurisdictions. Export / import prices for certain commodities (e.g. oil products, precious metals) are also within the scope of the Russian transfer pricing rules.

Taxpayers need to prepare transfer pricing documentation on an annual basis in Russia, and a local benchmarking study is required when testing the profitability of a Russian company. In addition, taxpayers are required to submit a notification on controlled transactions by 20 May following the reporting year.

Advance Pricing Agreements (APAs) are available in Russia, but the practice is not extensive.

Transfer pricing study snapshot

The purpose of a transfer pricing study

	Applicable	Submission to tax authority required	Thresholds apply/exist
Legal requirements	●	●	●
Protection from penalties	●	●	
Reduce risk of adjustment	●	●	
Shifts burden of proof	●	●	

Basic information

Tax authority name

Federal Tax Service (FTS).

Citation for transfer pricing rules

- Chapter 14.1. (Articles 105.1-105.2 of the Russian Tax Code) — Related parties
- Chapter 14.2. (Articles 105.3-105.6 of the Russian Tax Code) — General provisions on prices and taxation. Information used for comparability analysis
- Chapter 14.3. (Articles 105.7-105.13 of the Russian Tax Code) — Transfer pricing methods
- Chapter 14.4. (Articles 105.14-105.16 of the Russian Tax Code) — Controlled transactions. Preparation and submission of documents for tax authority monitoring. Notification of controlled transactions
- Chapter 14.5. (Articles 105.17-105.18 of the Russian Tax Code) — Tax control of prices between related parties

- Chapter 14.6. (Articles 105.19-105.25 of the Russian Tax Code) — Advance pricing arrangements
- Articles 129.3-129.4 of the Russian Tax Code — Penalties; and
- Certain articles of Chapter 25 of the Russian Tax Code stipulate specific transfer pricing rules for securities and derivatives (Article 280 of the Russian Tax Code) and interest (Article 269 of the Russian Tax Code).

Effective date of transfer pricing rules

1 January 2012.

What is the relationship threshold for transfer pricing rules to apply between parties?

More than 25 percent direct/indirect ownership of one company by another company including parties in which one company participates directly or indirectly and such participation exceeds 25 percent (sister companies).

Moreover, the definition of related parties also includes:

- parties that are controlled by the same CEO or board of directors, 50 percent of which are the same persons
- parties where one party has the right to appoint the CEO for the other party or at least 50 percent of the board of directors for the other party
- party and an individual where the individual performs the duties of the party's chief executive officer
- parties and/or individuals, if the share of direct participation of each preceding party in each subsequent organization equals more than 50 percent
- individuals, if one individual is subordinate to another individual by official position
- an individual, his or her spouse, parents (including adoptive parents), children (including adopted children), full and half brothers and sisters; and
- a trustee and ward by a court decision on related party status.

What is the statute of limitations on assessment of transfer pricing adjustments?

The tax authorities can audit only three calendar years preceding the year in which the decision to conduct a transfer pricing audit was taken by the transfer pricing authority.

The new transfer pricing rules also stipulate certain transitional provisions for 2012-2013:

- a decision to conduct a tax audit of controlled transactions performed in 2012 can be taken no later than 30 June 2014 (amendments to the transfer pricing legislation of April 2013); and
- a decision to conduct a tax audit of controlled transactions performed in 2013 can be taken no later than 31 December 2015.

Transfer pricing disclosure overview

Are disclosures related to transfer pricing required to be submitted to the revenue authority on an annual basis (e.g. with the tax return)?

Yes. A taxpayer must submit notification to the tax authorities about controlled transactions that occurred in each calendar year by 20 May of the following year.

What types of transfer pricing information must be disclosed?

The form of the taxpayer's notification is rather complex and contains the following main fields:

- calendar year in which a transaction subject to the transfer pricing regulations occurred
- subject matter of the transaction
- information about the parties to the transactions, (name, taxpayer's identification number)
- income received and expenses incurred relating to the transaction
- grounds for classifying the transactions as controlled
- pricing methods used by the taxpayer (optional); and

- information sources used by the taxpayer (optional).

When providing information on the subject matter of the transaction, it will be necessary not only to give a full description (e.g. goods, works, services, or property rights), but also to submit more detailed data, including the code for the subject matter of the transaction in accordance with one of three classifications:

- TNVED (Foreign Economic Activity Commodity Nomenclature) — for cross-border transactions with goods
- OKP (Russian Classification of Products) — domestic transactions for goods; and
- OKVED (Russian Classification of Economic Activities) (for works, services, or property rights) — for services and other transactions.

The most detailed information is required for transactions with goods where the taxpayer will have to inform the tax authority additionally of:

- the country of origin, shipping (loading) point
- delivery (discharging) point; and
- as well as the terms of delivery.

Please note that the above information should be provided for each transaction. As a result, companies usually prepare and file a transfer pricing notification in the electronic format.

What are the consequences of failure to submit disclosures?

Failure to submit notification to the tax authorities about controlled transactions or the disclosure of incorrect data may result in fine of 5,000 Russian rubles (RUB) per taxpayer. Also, failure to submit notification increases likelihood of transfer pricing audit (in case local tax inspectorate informs Federal Tax Service about controlled transactions of the taxpayer).

Transfer pricing study overview

Can documentation be filed in a language other than the local language? If yes, which ones?

No.

When a transfer pricing study is prepared, should its content follow Chapter V of the Organisation for Economic Co-operation and Development (OECD) Guidelines?

No. Transfer pricing documentation can be presented in any format, but under the Tax Code should contain the following details:

- indication of the parties to the transaction and their residence, description of their functions, assets and risks attributable to the transactions
- description of the transaction: subject matter, terms and conditions, methodology applied, etc.
- justification of the transfer pricing method applied: indication of sources of information used, calculation of the range of arm's length prices/profitability, amount of income received and/or expenses incurred relating to the transactions and related economic benefits received
- description of adjustments to the tax base (if any) performed by the taxpayer
- other information necessary to justify the transfer prices used.

Transfer pricing documentation should be prepared with references to the Russian tax code (rather than the OECD transfer pricing Guidelines). A local benchmarking analysis is usually required.

In addition, the Russian tax authorities published for taxpayers Guidelines on preparing transfer pricing documentation. It is strongly recommended to prepare local transfer pricing files in accordance with these Guidelines.

Does the tax authority require an advisor/tax practitioner to have specific designation in order to prepare or submit a transfer pricing study?

No.

Transfer pricing methods

Does your country follow the transfer pricing methods outlined in Chapter II of the OECD Guidelines? If exceptions apply, please describe.

No. Under the Tax Code, the Resale Price Method is a priority method for goods, which were purchased in a controlled transaction and resold to the independent party. The CUP method requires a high degree of comparability for its application. In the case where general transfer pricing methods (or a combination thereof) cannot be applied, the market price for non-recurring transactions (e.g. sale of a trademark) could be determined using an independent appraisal report.

Transfer pricing audit and penalties

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? And if so, how many days?

Yes, 30 days.

When the tax authority requests a taxpayer's transfer pricing documentation, are there timing requirements for a taxpayer to submit its documentation? Please explain.

The taxpayer must provide the transfer pricing documentation to the tax authorities within 30 working days from the date of the tax authorities' request.

If an adjustment is proposed by the tax authority, what dispute resolution options are available?

Upon the audit, the tax authorities issue the act summarizing the audit results. The taxpayer is able to provide their appeal to this act. Then, the tax authorities take the decision on the transfer pricing audit. If the taxpayer does not agree with the decision, the tax authorities will try to enforce it via a litigation procedure in the Russian arbitration court.

If an adjustment is sustained, can penalties be assessed? If so, what rates are applied and under what conditions?

If a transfer pricing adjustment results in an additional tax liability, the taxpayer is subject to late payment interest of 1/300 of the currently effective refinancing rate established by the Central Bank of the Russian Federation (8.25 percent as of 1 July 2015).

The penalty for underpayment of tax arising from non-compliance with the transfer pricing regulations is 40 percent of the underpaid tax. This penalty applies starting from 2017. For 2012-2013, the penalty is not applied. For 2014-2016, the penalty will be 20 percent of the underpaid tax.

To what extent are transfer pricing penalties enforced?

Penalties are generally enforced in practice.

What defenses are available with respect to penalties?

If a taxpayer makes a transfer pricing self-adjustment and pays additional tax liabilities and late payment interest prior to the tax audit, no penalties should apply.

A taxpayer is exempt from 20 percent/40 percent penalty if the relevant transfer pricing documentation supporting arm's length level of prices was properly prepared and provided to the tax authorities within 30 working days upon receiving their request.

What trends are being observed currently?

During transfer pricing audits the Federal Tax Service mainly focus on cross-border transactions. From our experience, they tend to apply the CUP method in transactions with commodities.

The local tax authorities generally pay much attention to intra-group transactions such as management services, IP royalty, interest deduction. They inter alia analyze substance of transactions and their proper document support. Also, Russian tax authorities may test the arm's length nature of prices in non-controlled transactions (i.e. transactions between unrelated parties) in case they assume unjustified tax benefit of the taxpayer.

Special considerations

Are secret comparables used by tax authorities?

No. Nonetheless, tax authorities may use secret comparables for selection of companies for transfer pricing audits.

Is there a preference, or requirement, by the tax authorities for local comparables in a benchmarking set?

A local study is required for testing profitability of Russian companies (a permanent establishment in Russia of a foreign company). For testing profitability of foreign companies, a foreign study may be accepted, but the search strategy in the study should be in line with requirements under the Russian Tax Code (e.g. requirement to reject loss-making companies etc.).

Do tax authorities have requirements or preferences regarding databases for comparables?

The results of benchmarking studies aimed at testing the arm's length nature of prices/margins of Russian companies (or foreign companies with a Russian permanent establishment) are more likely to be acceptable if the data for the search were obtained from Russian databases (i.e. SPARK, RUSLANA, etc.).

To test the arm's length nature of prices/margins of European companies, the Amadeus database can be used.

Does the tax authority generally focus on the interquartile range in a TNMM analysis?

Yes, always.

Does the tax authority have other preferences in benchmarking? If so, please describe.

Please note that the Russian Tax Code contains a special formula for calculating the arm's length range. This formula is slightly different from the interquartile range.

What level of interaction do tax authorities have with customs authorities?

There is some interaction, but it is generally limited.

Are there limitations on deductibility of management fees beyond the arm's length principle?

Yes. They must be supported by documentation evidencing the fact that services were actually rendered and that a Russian taxpayer received the economic benefit from such services.

Are management fees subject to withholding?

No.

Are there limitations on the deductibility of royalties beyond the arm's length principle?

Yes. There should be economic justification of the royalty payment. There are certain court decisions arguing the economic substance of royalty payment outside of Russia.

Are royalties subject to withholding?

Yes.

Are taxpayers allowed to file tax return numbers that differ from book numbers?

Yes. If a company underestimated its tax base due to non-arm-length prices and confirm this during preparation of transfer pricing documentation, the company is required to make a self-adjustment in the tax return.

For cross-border transactions true down adjustments (i.e. adjustments to decrease the tax base in Russia) are generally not feasible due to tax and customs issues and prohibited as such under Russian transfer pricing rules. True-up adjustments should be carefully structured as various options can be considered.

For domestic transactions starting from 2015, the mechanism of correlative adjustments is introduced.

Other unique attributes?

None.

Tax treaty/double tax resolution

What is the extent of the double tax treaty network?

Extensive.

If extensive, is the competent authority effective in obtaining double tax relief?

The Russian competent authority has little experience in transfer pricing matters.

When may a taxpayer submit an adjustment to competent authority?

No formal rules exist in this area.

May a taxpayer go to competent authority before paying tax?

No formal rules exist in this area.

Advance pricing agreements

What APA options are available, if any?

Unilateral, bilateral, multilateral.

Is there a filing fee for APAs?

Yes. The fee for concluding a unilateral APA is RUB2 million.

Does the tax authority publish APA data either in the form of an annual report or through the disclosure of data in public forums?

No.

Are there any difficulties or limitations on the availability or effectiveness of APAs?

Yes. APAs are available only for 'large taxpayer'. The general qualification criteria for a 'large taxpayer' varies depending at which level (federal or regional) such taxpayer is subject to tax administration. A taxpayer is generally considered a 'large taxpayer' at the regional level if any of the following criteria is met:

- total amount of annual federal taxes equals RUB1 billion; or
- total annual revenue equals RUB1 billion to RUB20 billion (amendment of Federal Tax Service dated 24 April 2012) of Federal Tax Service dated 24 April 2012).

The qualification criteria for a 'large taxpayer' at the federal level are even higher.

The practice of APA develops in Russia. According to the official information, the 1st APA was concluded by an oil company, Rosneft, in November 2012. Under this agreement, Rosneft and the Federal Tax Service agreed on certain pricing methods for oil sales

transactions in the domestic market. As of July 2015, more than 20 APAs were concluded, mostly on domestic Russian transactions. KPMG Russia has an extensive practical experience on obtaining APAs in Russia.

KPMG in Russia

Natalia Valkovskaya

Tel: +7 495 937 4477 (ext. 13766)

Email: nvalkovskaya@kpmg.ru

As email addresses and phone numbers change frequently, please email us at transferpricing@kpmg.com if you are unable to contact us via the information noted above.

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