Korpus Prava

#3 / Autumn, 2020

Analytics

Tax & Law Journal for Top Executives

— Change is good.
— Yeah, but it's not easy.

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Amendments to double taxation conventions. Process is set in motion

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Московская государственная юридическая академия
МГЮА

Dear readers!

We are glad to welcome you to our new edition of "Korpus Prava.Analytics".

Articles of the autumn edition written by our specialists answer interesting and topical questions.

At the end of March, the Ministry of Finance of the Russian Federation began to implement the order of the President of the Russian Federation to approve amendments to double taxation conventions (DTC) with certain jurisdictions. Thus, in September, an agreement on new terms was reached with Cyprus. For more information about new business conditions, read the article by senior lawyer Anna Senchenko.

Since 2020, currency individual residents of the Russian Federation are required to submit notices to the tax authorities on opening / closing / changing details of accounts opened not only with foreign banks, but also with other financial institutions. In his article Aleksey Oskin tried to cover the meaning of the "financial market organization" in as much detail as possible.

Since September 1, 2020, the procedure of out-of-court bankruptcy for individuals regarding debts amounting from 50 to 500 thousand rubles has become possible. The article by Mikhail Oberemkov describes conditions of participation in this procedure, its features and consequences.

After some time, we decided to return to the topic of digital currency and digital financial assets, because this July the federal law was published introducing rules for DFA regulation. For more information on this issue, see the article by junior lawyer Ekaterina Sechkareva.

We hope this feature material will be really beneficial for you. We look forward to your recommendations and questions, and we will do our best to cover them in our next edition or news feed on our website or Facebook page.

Enjoy the reading!

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DIGITAL FINANCIAL ASSETS

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On July 31, Federal Law No. 259-ФЗ "On Digital Financial Assets, Digital Currency and Amendments to Certain Legislative Acts of the Russian Federation" (hereinafter, the Law) was published.

This regulatory legal act has been significantly revised since its adoption by the State Duma of the Russian Federation in the first reading on May 22, 2018. Thus, a virtually new version of the Law was developed for the second reading. Initially, it was planned to essentially ban the issue and turnover of cryptocurrencies and determine liability for any direct or indirect participation in such activities. However, such strict measures caused criticism from business and experts, so they were not included in the final version of the law (which does not exclude the possibility of introducing such measures later by separate acts).

Simultaneously, FATF[1] considered turnover of tokens and cryptocurrencies, and certain recommendations were developed for making amendments to the national legislation. As a result, at the beginning of this year, the draft law was passed in the second reading with significant amendments regarding regulation of cryptocurrencies.

The law shall become effective on January 1, 2021 (except for certain provisions) and shall define digital financial assets (hereinafter, DFA) as digital rights that include, inter alia:

- Monetary claims;
- Ability to exercise rights associated with equity securities;
- Participation interest in the capital of non-public JSC.

DFA may be issued, recognized and traded only by making (changing) entries in the information system based on the distributed ledger (blockchain), and in other information systems.

DFA shall be issued under a resolution on the issue. It shall specify the type and scope of rights that are certified by the issued DFA, and other information. A resolution on the issue shall be posted on the website of the DFA issuer, and on the website of the operator of the issuing information system. A resolution on the issue may be recognized as a public offer if it is addressed to the general public. A resolution on the issue of DFA certifying the ability to exercise rights associated with equity securities or certifying the

1. Financial Action Task Force on Money Laundering (FATF) is an intergovernmental organisation that develops global standards for anti-money laundering measures and combating the financing of terrorism (AML/CFT), and evaluates the compliance of 228 national AML/CFT systems with these standards.

right to claim transfer of equity securities or certifying the participation interest in the capital of a non-public JSC shall not be addressed to the general public.

DFA shall be accounted for in the issuing system. As a general rule, records on DFA may be entered or changed by order of the person that issued such assets, as well as their owner. Individuals registered as individual entrepreneurs and legal entities (commercial and non-commercial organizations) are entitled to make entries on the issue of digital financial assets in the information system. One may access the system only with a unique code, and a resolution on the issue shall be executed in e-form and signed with an enhanced qualified digital signature. Moreover, a resolution on the issue of DFA should be publicly available on the Internet until the obligations to all asset holders are fully fulfilled. The Bank of Russia is entitled to determine attributes of DFA that may be acquired by unqualified investors, and to limit the amount of their investments in such assets.

It is allowed to make transactions with cryptocurrency, but at the same time it is forbidden to use it as a payment instrument. The law contains no limited list of transactions that are allowed to be made with DFA. However, the purchase and sale of DFA, as well as the exchange of DFA of one type for the same assets of another type (including DFA issued under the foreign legislation, and digital rights that include both DFA and other digital rights) are mentioned separately.

Transactions shall be concluded via the exchange operator. These mainly include banks and stock exchanges. However, other legal entities that are included by the Bank of Russia in the register thereof may become such operators.

The circle of DFA purchasers is not limited by the Law. However, the Law separately provides for the right of the Bank of Russia to determine characteristics of DFA that may only be acquired by qualified investors and/or attributes of DFA that may be acquired by non-qualified investors only within the amount of cash and/or total cost of other DFA transferred as consideration set by the Bank of Russia.

Therefore, the Law will allow to convert traditional financial instruments into a digital form and increase the number of ways to attract investments. Cryptocurrencies will get the status of a standard financial asset and become a way to invest available money. It is not the last regulatory act that will regulate cryptocurrencies, because in autumn a more detailed draft law is planned to be introduced that is likely to define the rules of mining, among other things. A

THROUGH COURT OR NOT, THAT IS THE QUESTION

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The bankruptcy procedure for individuals is a much rarer phenomenon than the bankruptcy of legal entities. However, occasionally, citizens, regardless of whether they are engaged in business activities, find themselves in the situation when they are unable to cope with their debts and are forced to follow such a lengthy procedure.

Starting from September 1, 2020, Federal Law No. 289-ФЗ "On Amendments to the Federal Law "On Insolvency (Bankruptcy)" and Certain Legislative Acts of the Russian Federation Regarding Out-of-Court Bankruptcy of Citizens" dated 31.07.2020 shall become effective. As the name suggests, this law offers the possibility for citizens to follow the bankruptcy procedure without filing a relevant petition to the arbitration court.

To that effect, a citizen shall meet a number of conditions introduced by the amended law, namely:

- The total amount of outstanding obligations (including obligations that are not yet due, alimony obligations and obligations under the suretyship agreement) is not less than 50 thousand and not more than 500 thousand rubles;
- Enforcement proceedings were terminated against him/her due to the absence of forfeitable property, after which no other enforcement proceedings were initiated.

If these conditions are met, the next step is to file a bankruptcy petition to the Multifunctional Centre. By filing a petition, a citizen confirms his/her compliance with the above conditions. Moreover, a citizen shall list all claims against him/her in such a petition that make up the number of outstanding obligations because of which the bankruptcy procedure is initiated.

It is crucially important for a debtor to list all possible claims, since in accordance with the general rule of the Federal Law "On Insolvency (Bankruptcy)" the deadline for fulfilling such claims will be deemed due, but most importantly, such claims will no longer incur a penalty, and after the successful completion of the bankruptcy procedure, a citizen will be released from the obligation to fulfill them. However, this rule does not apply to requirements that are not specified in the citizen's petition. Therefore, if any claims are not specified in the petition both during the entire bankruptcy procedure and after it, they will continue to incur penalties, and a debtor will not be exempt from the obligation to fulfill them. Moreover, such creditors shall be entitled to apply to the arbitration court with a bankruptcy petition against

a debtor on general terms during the entire out-of-court bankruptcy procedure.

It is also worth noticing that the out-of-court bankruptcy procedure is not a "cure-all" for debtors, since the new law limits types of obligations from which a citizen may be exempt upon its completion. Thus, a citizen shall not be released out of court from the obligation to fulfill the claims:

- For current payments;
- For compensation for personal injuries;
- For payment of wages and severance pay;
- Other claims that are inextricably linked to the creditor's identity;
- For bringing a citizen to subsidiary responsibility as a controlling person;
- For compensation for losses caused to a legal entity with a citizen being its participant;
- For compensation for property damage caused intentionally or by gross negligence;
- For consequences application of invalidity of a suspicious transaction or a transaction that entails giving preference to one of the creditors over others.

The Ministry of Economic Development describes the innovation as "assistance to the least advantaged citizens who got into a difficult situation in freeing from debts and returning to a normal life". Indeed, this procedure is a kind of step towards bona fide debtors who are objectively aware of their insolvency. It allows such debtors to both get free from their debt obligations relatively quickly and reduce the burden on arbitration courts.

At the same time, out-of-court bankruptcy leaves virtually no loopholes for mala fide debtors, i. e. there is no exemption from obligations if a debtor was brought to administrative or criminal liability for wrongful actions upon bankruptcy, deliberate or fictitious bankruptcy (under the bankruptcy proceedings), or if upon the occurrence or performance of obligations, on which the claims of the scheduled creditor are based, a debtor acted illegally (committed fraud, provided information known to be false when obtaining a loan, intentionally destroyed property, and committed other similar actions).

Upon completion of the out-of-court bankruptcy procedure, a citizen faces the same consequences as after a usual bankruptcy procedure:

- A citizen is unable to be registered as an individual entrepreneur for 5 years (if at the time of bankruptcy he was an individual entrepreneur);
- A citizen has no right to assume obligations under credit agreements or loan agreements without disclosing the fact of his/her bankruptcy for 5 years;
- A citizen has no right to hold administrative positions and generally participate in the management of a legal entity (for 3 years for ordinary legal entities; for 5 years for insurance companies, non-state pension funds, managing companies of investment funds, mutual funds or microfinance companies; for 10 years for credit organizations).

Debtors should keep in mind that if a citizen receives any property (as a gift, inheritance, etc.) sufficient for full or substantial discharge of the claims specified in the petition during the out-of-court bankruptcy procedure, he/she should notify the Multifunctional Centre thereon within 5 business days. In this case, the procedure will be terminated.

It is also important to mention that after the completion of the out-of-court bankruptcy procedure, a citizen may re-apply to the Multifunctional Centre with an out-of-court bankruptcy petition only after 10 years.

Therefore, there are the following stages of out-of-court bankruptcy (fig. 1).

Advantages of the procedure:

- Free of charge nature (the cost of the court procedure is often huge for an insolvent debtor — starting from 100,000 rubles). Given that a debtor filing a bankruptcy petition is extremely limited in funds, this advantage is the most significant;
- Simplicity (all that is required from a debtor is to execute a petition and list

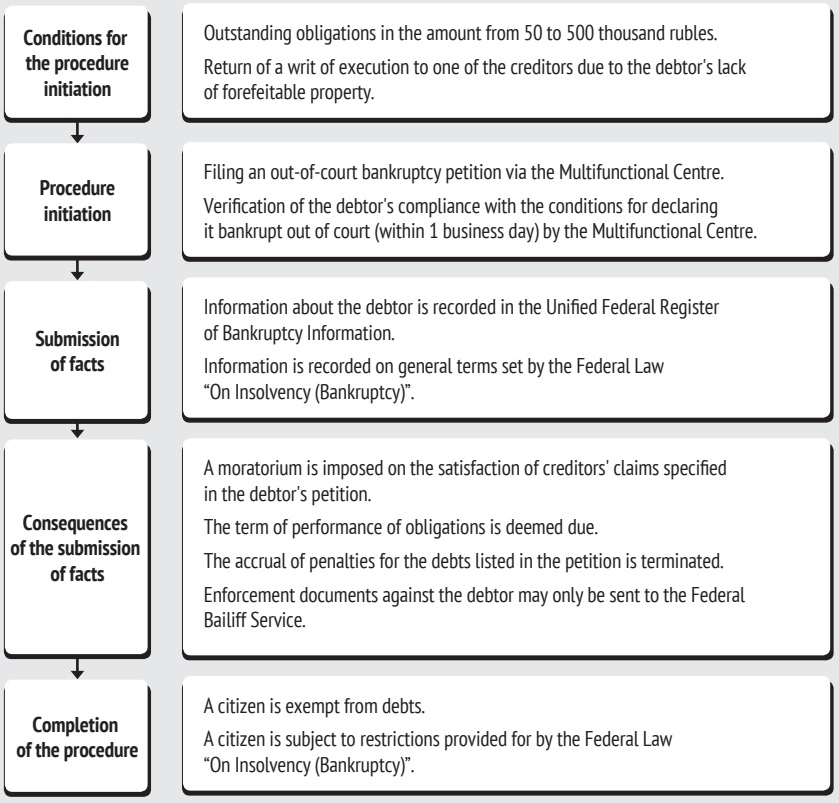

Fig. 1.

all the debts therein; the further procedure will be carried out without his/her participation, and there is no need to search for a financial manager);

- Quick consideration (the new procedure is carried out within 6 months, while bankruptcy proceedings in the arbitration court may take years).

Disadvantages of the procedure:

- A debtor is subject to restrictions not only after the procedure, but also during it (particularly, during the period of out-of-court bankruptcy, he/she is prohibited to receive loans, credit facilities, issue guarantees and perform other security transactions);
- Conditions for admission to the procedure: in addition to the requirements for the amount of outstanding claims, an obstacle to the exemption from debts out of court for a debtor will be obligatory performance and completion of enforcement proceedings on the relevant grounds;
- Long term restrictions on filing another petition.

Other disadvantages are reduced to adverse bankruptcy consequences above, but they coincide with those upon the court bankruptcy and are irrelevant in the context of comparing the two procedures.

The out-of-court bankruptcy procedure is an innovation designed to simplify lives of citizens who are objectively unable to cope with debts and honestly admit it. Out-of-court bankruptcy is introduced both to reduce the burden on the judicial system, and to encourage the bona fide behavior of debtors in particular, and civil transactions in general. However, only time will show how effective and applicable this innovation is going to be in real terms.

AMENDMENTS TO PROVISIONS GOVERNING LIABILITY FOR VIOLATIONS OF THE CURRENCY LEGISLATION OF THE RUSSIAN FEDERATION

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From July 31, 2020, Federal Law No. 218-ФЗ "On Amendments to Articles 3.5 and 15.25 of the Code of Administrative Offences of the Russian Federation" dated 20.07.2020 became effective and amended provisions governing liability for violations of the currency legislation.

In some cases, liability for violations of the currency legislation was mitigated (and even abolished), while in some cases additional grounds and penalties were introduced.

For greater clarity, the table below contains information on all types of liability set for violations of the legislation on currency regulation and currency control:

Table 1

Provision of the Russian Code of Administrative Offences	Type of violation	Extent of liability Before	After	Nature of changes
Part 1, article 15.25	Illegal foreign exchange transactions	From 75% to 100% of the illegal foreign exchange transaction amount		No amendments
Part 2, article 15.25	Violation of the deadline for submitting notices (on opening/closing/ changing details) for foreign accounts	For citizens — from 1 to 1.5 thousand rubles, for officials — from 5 to 10 thousand rubles, for legal entities — from 50 to 100 thousand rubles		Liability for violation of the deadline for submitting notices (on opening/closing/ changing details) for brokerage accounts is introduced

Table 1 (continuance)

Provision of the Russian Code of Administrative Offences	Type of violation	Extent of liability Before	After	Nature of changes
Part 2.1, article 15.25	Failure to submit notices (on opening/ closing/ changing details) for foreign accounts	For citizens — from 4 to 5 thousand rubles, for officials — from 40 to 50 thousand rubles, for legal entities — from 800 thousand rubles to 1 million rubles		Liability for failure to submit notices (on opening/ closing/ changing details) for brokerage accounts is introduced
Part 4, article 15.25	Non-compliance with requirements for repatriation of foreign currency earnings	For citizens and legal entities — 1/150 of the key rate of the Central Bank of the Russian Federation for each day of delay and/or from three-quarters to one amount of non-credited funds, for officials — from 20 to 30 thousand rubles	For citizens and legal entities: 1. Penalty amounting to 1/150 of the key rate of the Central Bank of the Russian Federation for each day of delay and/or 2. Penalty on the amount not credited in due time: • from 3% to 10% (for foreign trade contracts in rubles); • from 5% to 30% (for foreign trade contracts and loan agreements in the foreign currency); For officials — from 20 to 30 thousand rubles	Liability is reduced
Part 4.1, article 15.25	Non-fulfilment of the obligation to ensure that the Russian currency is credited to accounts in the	For individual entrepreneurs and legal entities — penalty in the amount from 40 to 50 thousand rubles, for officials — from 20 to 30 thousand rubles		No amendments

Table 1 (continuance)

Provision of the Russian Code of Administrative Offences	Type of violation	Extent of liability Before	After	Nature of changes
	Russian Federation under foreign trade contracts for which a transaction certificate is required in the amount determined by the Government of the Russian Federation			
Part 4.2, article 15.25	Non-compliance with the requirements for the repatriation by a professional participant of foreign economic activities	No previous provisions	For individual entrepreneurs and legal entities — from 3% to 5% of the amount not credited in due time; for officials — from 20 to 30 thousand rubles	No previous provisions. Therefore, liability for professional participants of foreign economic activities is mitigated
Part 4.3, article 15.25	Non-fulfillment of obligations (not related to currency repatriation) for foreign trade transactions, if such transactions are subject to the requirements of the currency legislation of the Russian Federation and enactments of the currency control authorities	No previous provisions	For individual entrepreneurs and legal entities — from 5% to 30% of the amount due to a resident from a non-resident; for officials — from 20 to 30 thousand rubles	No previous provisions. Therefore, new penalties for violation of the currency legislation is introduced
Part 5, article 15.25	Non-fulfillment of the obligation to return funds to the Russian Federation for non-imported goods, non-rendered services, etc.	For citizens and legal entities — 1/150 of the key rate of the Central Bank of the Russian Federation for each day of delay and/or from three-quarters to one amount of funds not returned	For citizens and legal entities — 1/150 of the key rate of the Central Bank of the Russian Federation for each day of delay and/ or a penalty on the amount not returned to the Russian Federation:	Liability is reduced

Table 1 (continuance)

Provision of the Russian Code of Administrative Offences	Type of violation	Extent of liability Before	After	Nature of changes
		to the Russian Federation, for officials — from 20 to 30 thousand rubles	• From 3% to 10% (for foreign trade contracts in rubles); • From 5% to 30% (for foreign trade contracts in the foreign currency); For officials — from 20 to 30 thousand rubles	
Part 5.1, article 15.25	Repetition of administrative offenses under parts 1, 4, 4.1, 4.3 and 5, article 15.25 of the Code of Administrative Offences of the Russian Federation by an official	Disqualification for a period from 6 months to 3 years		No amendments
Part 5.2, article 15.25	Actions (inaction) under parts 4, 4.1, 4.2, 4.3 and 5, article 15.25 of the Code of Administrative Offences of the Russian Federation, if the amount of non-credited (credited with violated deadlines) funds exceeds 100 million rubles a year	For citizens and legal entities — 1/150 of the key rate of the Central Bank of the Russian Federation for each day of delay and/or from three-quarters to one amount of funds not returned to the Russian Federation, for officials — from 40 to 50 thousand rubles or disqualification for a period from 6 months to 3 years		No amendments
Part 6, article 15.25	Non-compliance with the procedure for submitting cash flow statements regarding foreign bank and brokerage accounts, as well as the procedure for fulfillment of other obligations	• For citizens — from 2 to 3 thousand rubles; • For officials — from 4 to 5 thousand rubles; • For legal entities — from 40 to 50 thousand rubles		1. Liability for non-compliance with the procedure for submitting cash flow statements

Table 1 (continuance)

Provision of the Russian Code of Administrative Offences	Type of violation	Extent of liability Before	After	Nature of changes
Part 6.1, article 15.25	Violation of deadlines for submitting cash flow statements regarding foreign bank and brokerage accounts by no more than 10 days	• For citizens — from 300 to 500 rubles; • For officials — from 500 to 1 thousand rubles; • For legal entities — from 5 to 15 thousand rubles		regarding foreign bank and brokerage accounts is introduced. 2. Liability for violation of deadlines and procedure for submitting accounting and reporting forms on foreign exchange transactions is excluded (if the delay is less than 90 days, see part 6.3.1, article 15.25 of the Code of Administrative Offences of the Russian Federation)
Part 6.2, article 15.25	Violation of deadlines for submitting cash flow statements regarding foreign bank and brokerage accounts by more than 10 days, but not more than 30 days	• For citizens — from 1,000 to 1,500 rubles; • For officials — from 2 to 3 thousand rubles; • For legal entities — from 20 to 30 thousand rubles		
Part 6.3, article 15.25	Violation of deadlines for submitting cash flow statements regarding foreign bank and brokerage accounts by more than 30 days	• For citizens — from 2.5 to 3 thousand rubles; • For officials — from 4 to 5 thousand rubles; • For legal entities — from 40 to 50 thousand rubles		
Part 6.3.1, article 15.25	Failure to submit to the authorized bank accounting and reporting forms on foreign exchange transactions, supporting documents and information upon performing foreign exchange transactions ninety days after the end of the due period	No previous provisions	• For citizens — from 2.5 to 3 thousand rubles; • For officials — from 4 to 5 thousand rubles; • For legal entities — from 40 to 50 thousand rubles	Liability for violation of the reporting procedure for foreign exchange transactions shall apply only in case of a delay by 90 days or more
Part 6.4, article 15.25	Repetition of an offense under part 6, article 15.25 of the Code of Administrative Offences of the Russian Federation	• For citizens — 10 thousand rubles; • For officials — from 12 to 15 thousand rubles; • For legal entities — from 120 to 150 thousand rubles.		No amendments

Table 1 (continuance)

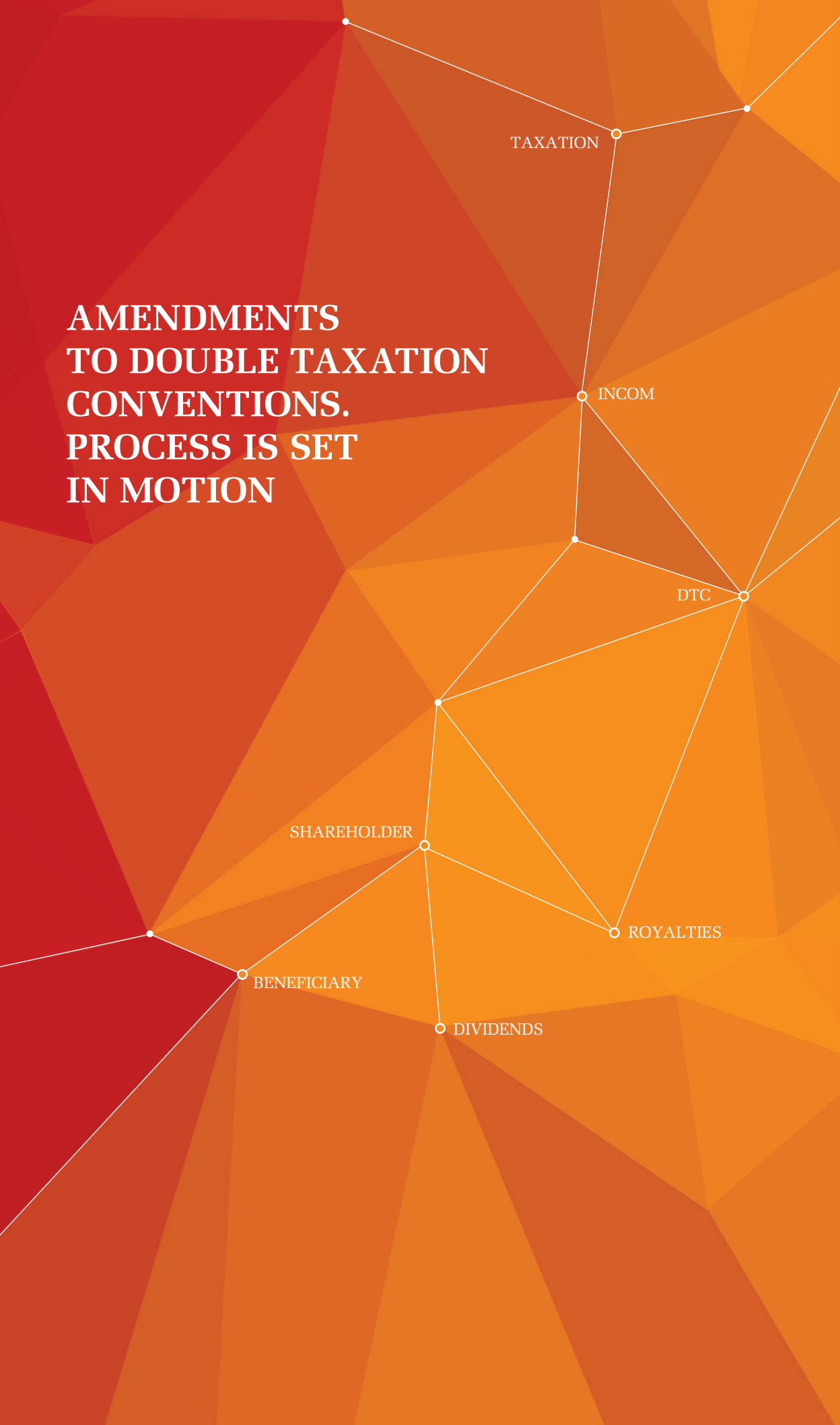
Provision of the Russian Code of Administrative Offences	Type of violation	Extent of liability Before	After	Nature of changes
	(except for submission of cash flow statements)			
Part 6.5, article 15.25	Repetition of an offense under part 6, article 15.25 of the Code of Administrative Offences of the Russian Federation in the form of non-compliance with the established procedure for submitting cash flow statements	• For citizens — 20 thousand rubles; • For officials — from 30 to 40 thousand rubles; • For legal entities — from 400 to 600 thousand rubles		No amendments

It is also worth noting that the new law includes the following grounds for exemption from liability for violations of the currency legislation:

1. A resident may be released from administrative liability for illegal foreign exchange transactions with a foreign account (part 1, article 15.25 of the Code of Administrative Offences of the Russian Federation) and non-compliance with requirements for repatriation (part 4, article 15.25 of the Code of Administrative Offences of the Russian Federation) when funds are credited to a foreign account bypassing a Russian account, provided that if within 45 days from the date of crediting funds to a foreign account they are transferred to an account in the authorized bank.
2. There is no administrative liability for non-compliance with requirements for repatriation (part 4, article 15.25 of the Code of Administrative Offences of the Russian Federation) if the amount of obligations does not exceed 200 thousand rubles.
3. Administrative liability established by parts 4 — 4.3, 5, 5.2 and 5.3, article 15.25 of the Code of Administrative Offences of the Russian Federation applies only upon the expiration of forty-five days after the expiration of the term for fulfilment of the relevant obligation in case of its non-fulfilment within the specified period.

Therefore, such amendments may be generally evaluated as positive. But notwithstanding the above, the scope of liability for certain types of violations of the currency legislation remains relatively high (from 75% to 100% of the transaction amount). In this regard, foreign currency residents of the Russian Federation still need to be careful when performing foreign exchange transactions, using foreign accounts, and entering into legal relations with currency non-residents of the Russian Federation.

AMENDMENTS TO DOUBLE TAXATION CONVENTIONS. PROCESS IS SET IN MOTION



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Not so long ago, changing terms of international taxation became a priority. The main objective is to prevent income siphoning to low-tax or tax-free jurisdictions by increasing the withholding tax rate in the Russian Federation.

If a party to the double taxation convention (hereinafter, DTC) accepts the terms proposed by the Russian Federation, the withholding tax rate at the source of dividends and interest income will increase up to 15%, otherwise the convention will be terminated, which will result in the inability to offset tax paid in one jurisdiction by another jurisdiction, and will lead to double taxation of international income.

Despite the fact that for DTC terms regarding royalties no amendments are planned, there is still a possibility of DTC termination, and in this case, instead of the reduced rate at the source and the possibility of setoff, a taxpayer will have to pay the withholding tax at the rate of 20% without a possibility to offset the tax amount.

Moreover, one of the consequences of DTC termination will be the absence of necessity to confirm the actual income recipient.

Currently, amendment letters have been sent to the following jurisdictions:

- Cyprus;
- Luxembourg;
- Malta.

It is also highly likely that the said instruction will affect the following jurisdictions:

- The Netherlands;
- Switzerland;
- Ireland.

If a written notice of termination of the Russian DTC is sent, changes will affect taxpayers no earlier than January 1, 2021. And in case of most jurisdictions, the Russian Federation should have sent such a notice by July 1, 2020, otherwise treaties will be deemed terminated only from January 1, 2022.

The parties were able to reach agreement on the DTC between the Russian Federation and the Republic of Cyprus, and they started the process of amending the convention.

Diagrams below show the consequences (fig. 1).

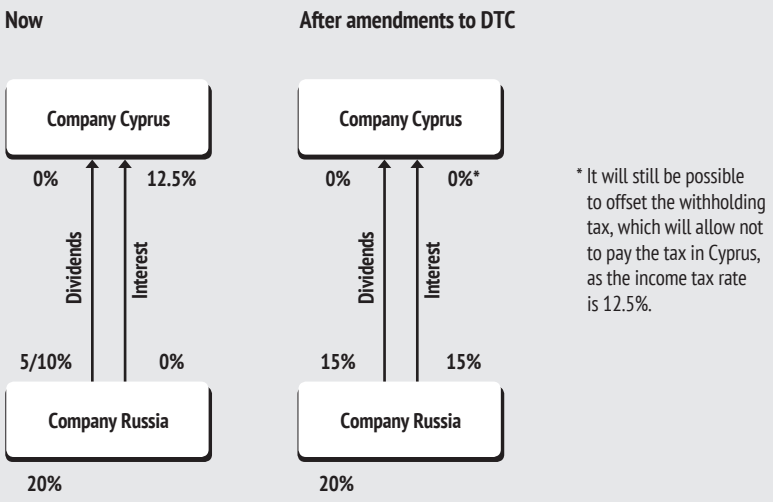

Fig. 1.

The following are options for consideration in this situation

1. Leave as is

This option is worth considering if a Cyprus company was created for purposes other than tax saving and/or tax saving is not a priority. Such a company could be created to protect assets, exploit peculiarities of the local legal system (e.g. the trust institution), and advantages that facilitate the process of attracting investors and/or making capital transactions. In such companies, the cash flow from assets in Russia is often minimal.

2. Apply a "pass-through" approach

This option suggests that the company ceases to recognize itself as an actual income recipient and, consequently, a tax agent at the source of income no longer applies the terms of the DTC with Cyprus, but rather the terms with an actual income recipient. One of the advantages of this option is cost reduction of creating and/or maintaining an actual income recipient status for a Cyprus company.

3. Terminate payment settlements

In case there are pending settlements between a Russian company and a Cyprus company in the current year, namely accrued interest, retained earnings, and accrued royalties.

4. Move to another place

Other jurisdictions may be worth considering. Currently, jurisdictions that provide comparable benefits (taking into account DTC and national legislation) are Luxembourg, Malta, and the Netherlands. However, when choosing a jurisdiction, one should keep in mind that the Ministry of Finance of the Russian Federation has already sent letters with a proposal to amend the DTC to Luxembourg and Malta. It is also highly likely that changes will affect the DTCs with the Netherlands, Switzerland, and Ireland. In addition to DTC provisions, one should consider such factors as the absence of the withholding tax and low tax burden on passive income when choosing a jurisdiction. In this situation, it is worth considering a comprehensive approach, particularly, moving to a jurisdiction with the territorial principle

of taxation (e. g. Hong Kong or Singapore) and applying a "pass-through" approach.

In addition, given the fact that the use of tax incentives becomes more and more complicated not only in Russia, but also worldwide, it seems reasonable to evaluate other benefits of jurisdictions not directly related to tax planning when moving to a different place, for example:

- Quality of the company administration;
- Cost of creating (moving) and maintenance of the company;
- Mechanisms for protecting rights of shareholders (e. g. obligatory registration of the transfer of ownership to shares in the state register);
- Possibility of obtaining tax residence, residence permit or passport through an investment in such a company;
- Reputation of the jurisdiction for AML regulatory and compliance purposes.

During such a transition period, it is recommended to take an inventory of the existing structure, evaluate all advantages and risks, benefits and costs, take into account non-monetary factors that may be significant, and perform one of the actions above, namely:

- Make payments that are able to be made;
- Evaluate the possibility of applying a "pass-through" approach to taxation;
- Evaluate the possibility of replacing a foreign company taking into account the indicated tendency to the DTC termination/amendment;
- Leave everything as is, if the DTC termination/amendment has no significant effect on the tax burden or obtaining tax savings is not the main purpose of creating a foreign structure.

At the same time, it is important to understand and remember that in this situation there is no common and multi-purpose solution. Despite the fact that all are now caught in the same storm, everyone keeps sailing their own boat, and the resolution to restructure will only be right if it takes into account specific goals and objectives of the beneficiary of the structure. A

FINANCIAL MARKET ORGANIZATIONS, WHAT ARE YOU?

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Since 2020, currency individual residents of the Russian Federation are required to submit notices to the tax authorities on opening (closing, changing details) accounts opened not only with foreign banks, but also with other financial institutions.

According to the Law "On Currency Regulation and Currency Control", other financial market organizations are organizations that in accordance with the personal law are entitled to provide services related to attracting funds from residents and allocating funds or other financial assets for holding, management, investment and/or execution of other transactions in the interests of a resident or directly or indirectly at the expense of a resident.

The wording is rather vague and, unfortunately, the law provides no public list of such organizations. However, the general meaning and the legislator's logic are quite clear.

Huge assets are accumulated on brokerage and investment accounts of citizens. Information thereon is received by the tax authorities via automatic exchange of tax information. It was a logical move to oblige citizens to disclose such information in their cash flow statements and statements on the flow of other assets on foreign accounts.

The ultimate question is which financial organizations are subject to the law on currency regulation and control.

Let us come back to the automatic exchange of information.

The Tax Code contains a list of financial market organizations that are required to disclose information on their clients via automatic exchange of tax information. Such organizations include:

- Credit institution;
- Voluntary life insurer;
- Professional participant in the securities market engaged in brokerage and/or securities management and/or depository activities;
- Manager under the property trust management agreement;
- Non-state pension fund;
- Equity investment fund;
- Managing company of the investment fund;
- Mutual fund or non-state pension fund;
- Central counterparty;
- Depository;
- Managing partner of an investment partnership;

- Other non-corporate organization or structure that accepts funds or other financial assets from clients for holding, management, investment and/or execution of other transactions in the interests of the client or directly or indirectly at the client's expense.

According to the Information of the Federal Tax Service dated April 19, 2019 containing "List of certain types of organizations classifiable as financial market organizations for the purposes of implementing Chapter 20.1 of the Tax Code of the Russian Federation" financial market organizations also include:

- Credit consumer co-operative;
- Agricultural credit consumer co-operative;
- Housing savings co-operative;
- Microfinance organization.

This information letter has a note stating that "This list represents the opinion of the Federal Tax Service of Russia approved by the Ministry of Finance of Russia and the Bank of Russia. The list is not exhaustive and will be supplemented; it does not constitute a regulatory legal act, is issued for informational purposes only and does not prevent organizations from following the legislation of the Russian Federation within the meaning that differs from the opinion contained herein."

Despite the note, it is worth being considered as a guide to action. In other words, if a currency resident of the Russian Federation joins a housing savings co-operative (or its equivalent) in the foreign territory, he/she is obliged to report thereon to the tax authority.

The main question remains, how to do this.

Notices on accounts have a number of fields to be filled in. For example, one of the mandatory fields is "Account Currency Code", "Account Number". Normally, brokerage accounts have no specific currency, and securities held on such accounts may be denominated in different currencies and their total value is not converted into one chosen currency.

As for investment insurance, such policies usually contain the number of the agreement itself, but such a policy has no separate account number.

It seems that these contradictions should be somehow considered by the legislator and the notice on opening (closing) an account (deposit) with a bank or another financial market organization located outside the Russian Federation should be modified taking into account that for different types of relations with financial market organizations not all information appearing in the established form should be specified.

The same applies to the cash and assets flow statement.

Currency residents will have to submit their first statements for 2020 in 2021. Although it is already relatively clear how to record a portfolio of securities in the statements, it is still not clear how to record, for example, an investment life insurance policy.

However, one thing is getting obvious. Conclusion of any agreement with a foreign organization to or from which a currency resident of the Russian Federation transfers or receives any asset entails the obligation to report this transaction to the tax authorities at the taxpayer's place of registration.

For quite some time now, citizens of the Russian Federation have been using such a financial service as investment life insurance. This option is also offered by our insurance companies, but many still buy policies from foreign insurers.

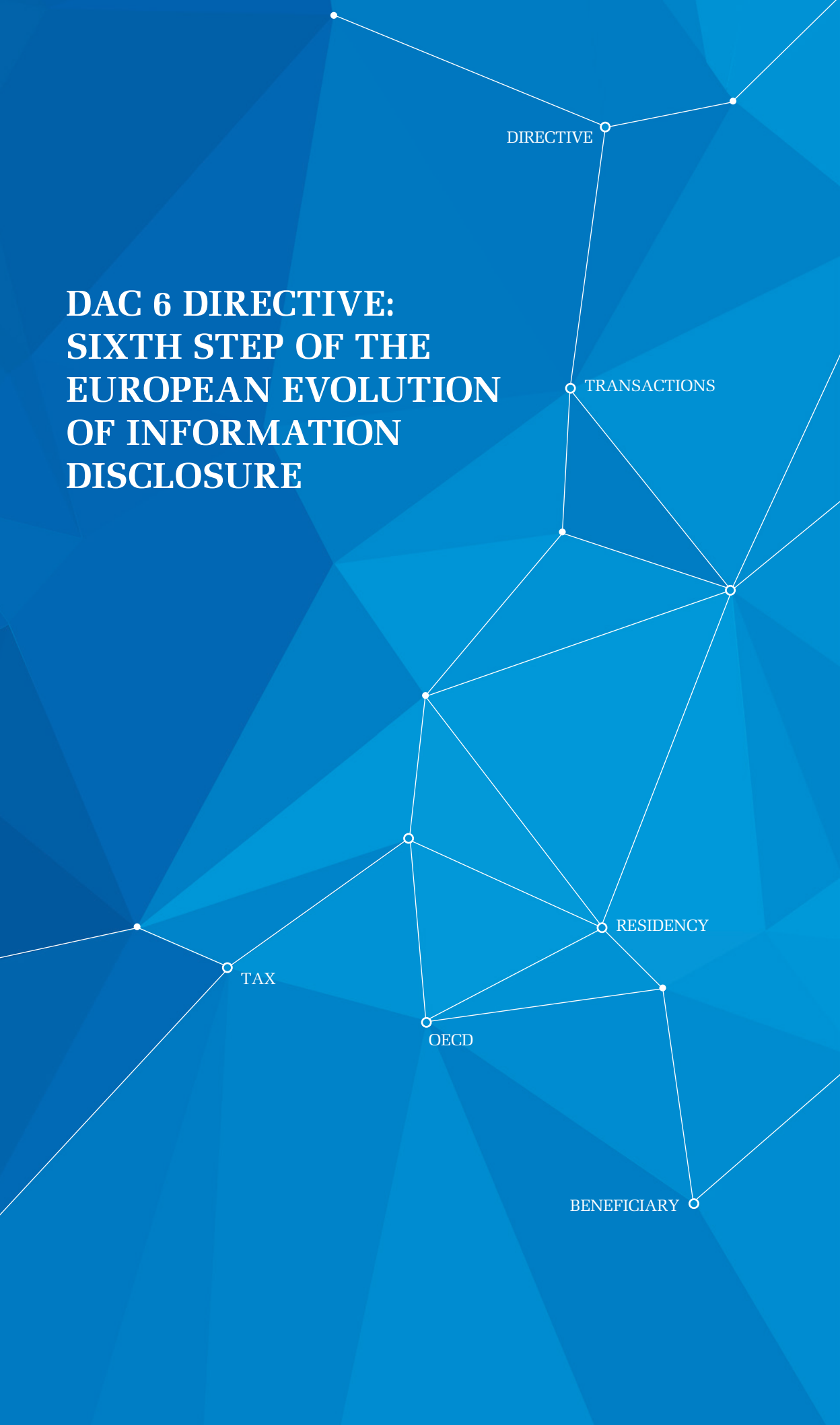
Investment insurance means that the insurance company uses the part of the funds that the client transfers to the insurer as premiums for investment purposes.

The client chooses a strategy and then upon the termination of the insurance policy he/she receives a guaranteed payment and remuneration on the investment.

Therefore, the insurer indirectly uses clients' funds to generate a profit, which directly turns its activities into the activities of the financial market organization. Accordingly, when purchasing an investment life insurance policy from a foreign insurance company, a currency resident of the Russian Federation should file a relevant notice.

It should be pointed out that the obligation to file notices on opening accounts with banks and other financial market organizations applies only to currency residents who have resided in the Russian Federation for more than 183 days. If a Russian citizen spends more than six months outside the Russian Federation, he/she is not required to file notices and cash flow statements for accounts opened with banks and other financial institutions.

DAC 6 DIRECTIVE: SIXTH STEP OF THE EUROPEAN EVOLUTION OF INFORMATION DISCLOSURE



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EU Council Directive 2018/822 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements was published on May 25, 2018. This Directive is also commonly referred to as DAC6 — Directive on Administrative Cooperation in (direct) taxation in EU, volume 6. This Directive is the sixth in a series of directives developed to encourage cross-border exchange of tax information in EU, and makes a part of step 12 in the BEPS Project (OECD base erosion and profit shifting project).

DAC 6 Directive provides for the obligation to disclose cross-border arrangements bearing hallmarks of aggressive tax planning to the tax authorities. According to EU aggressive tax planning means reduction of tax obligations by taxpayers via arrangements that may be technically legal, but their substance contradicts the letter of the law. Aggressive tax planning is also reflected in the use of loopholes in the tax system and inconsistencies between tax systems, which may lead, for example, to double tax evasion.

As mentioned above, in accordance with DAC 6 information on cross-border arrangements implemented by companies located in EU and bearing hallmarks of aggressive tax planning shall be disclosed. Such hallmarks are listed in Annex IV to DAC 6 and are divided into the following categories:

- Generic hallmarks linked to the main benefit test;
- Specific hallmarks linked to the main benefit test;
- Specific hallmarks related to cross-border transactions;
- Specific hallmarks concerning the automatic exchange of information and beneficial ownership;
- Specific hallmarks concerning transfer pricing.

A non-exhaustive list of hallmarks is given in the table 1.

An arrangement is recognized as cross-border if its participants are located in more than one Member State or in a Member State and a third country, and it meets at least one of the following criteria:

- Not all participants are tax resident in the same jurisdiction;
- At least one participant is a dual tax resident;
- At least one participant carries on a business in another jurisdiction through a permanent es-

Table 1

Generic hallmarks linked to the main benefit test	**Specific hallmarks linked to the main benefit test**	**Specific hallmarks related to cross-border transactions**	**Specific hallmarks concerning the automatic exchange of information and beneficial ownership**	**Specific hallmarks concerning transfer pricing**
Confidentiality provision based on which it is not allowed to disclose to intermediaries or to the tax authorities how the arrangement could secure a tax advantage	Acquisition of a loss generating company, discontinuing its main activities and using losses of the company to reduce its tax liabilities, including a transfer of its losses to another jurisdiction	An arrangement that involves deductible cross-border payments between associated companies when at least one of the following conditions is met: • The recipient of the payment is not a tax resident in any tax jurisdiction; • The recipient of the payment is a tax resident in a jurisdiction with zero/low taxation or a jurisdiction included in a list of non-cooperative jurisdictions of the EU or the OECD; • The payment benefits from a full exemption from tax in recipient's tax jurisdiction; • The payment benefits from a preferential tax regime in recipient's tax jurisdiction	Arrangements aimed at evasion from provisions on the automatic exchange of information: • The use of an account, product or investment that is not a Financial Account but has its features; • Transferring a Financial Account to a jurisdictions that has no effective provisions on the automatic exchange of information; • The reclassification of income and capital into products or payments that are not subject to the automatic exchange of information, etc	Arrangements involving the use of safe harbour rules that exempt a certain category of taxpayers or transactions from general rules of transfer pricing in a particular country

Table 1

Generic hallmarks linked to the main benefit test	Specific hallmarks linked to the main benefit test	Specific hallmarks related to cross-border transactions	Specific hallmarks concerning the automatic exchange of information and beneficial ownership	Specific hallmarks concerning transfer pricing
Provision on receipt / absence / reimbursement of a fee depending on the amount of received/ non-received tax advantage	Converting income into the category of income taxed at a lower level or exempt from tax	Claiming for depreciation amounts on the same asset in more than one jurisdiction	Arrangements with a non-transparent assets ownership chain: entities do not carry on a substantive economic activity supported by adequate staff, equipment, assets and premises; where the beneficial owner is made unidentifiable, etc	Arrangements involving the transfer of intangibles between associated companies that are hard to value due to a lack of comparable assets in the market, and high uncertainty in the estimation of the future income from such an asset
Standardised documentation and/or structure available to various taxpayers	Circulation of funds between intermediaries with no other commercial function, or making transactions for the purpose of offsetting or paying off obligations	Claiming relief for double taxation for the same item of income or capital in more than one jurisdiction		Arrangements involving an intra group cross-border transfer of functions and/or risks and/or assets if the projected EBIT during the three-year period after the transfer of the transferor(s) are less than 50% of the projected annual EBIT of such transferor(s) if the transfer had not been made
		The transaction provides for asset transfer, and consideration for such assets significantly varies in different jurisdictions		

tablishment situated in that jurisdiction and the arrangement forms part or the whole of the business of that permanent establishment;
- At least one participant carries on activities in another jurisdiction without being resident or creating a permanent establishment situated in that jurisdiction;
- The arrangement has a significant impact on the automatic exchange of information or the identification of beneficial ownership.

The information on arrangements which should be disclosed in accordance with DAC 6 includes:
- Identification data of intermediaries and taxpayers, including their names, date and place of birth (for individuals), details of tax residency, taxpayer identification number, and, if applicable, details of companies associated with taxpayers;
- Details of hallmarks listed in Annex IV to DAC 6 and mentioned above;
- General details of the cross-border arrangement without disclosure of commercial, industrial or professional secrets or trade process, and information that would contradict the public order;
- Date of the first step of the arrangement implementation;
- Value (amount) of the arrangement;
- National provisions forming the basis of the arrangement;
- Details of the Member States involved in the arrangement;
- Details of any other person in Member States likely to be affected by the arrangement.

The obligation of information disclosure is vested upon intermediaries, and in case there are no intermediaries or DAC 6 provisions do not apply to intermediaries for any reason, upon taxpayers themselves. Who are intermediaries? In DAC 6 an intermediary is defined as any person that designs, markets, organises or makes available for implementation or manages the implementation of a reportable cross-border arrangement. An intermediary should either:
- Be a resident in a Member State;
- Have a permanent establishment in a Member State through which the services in respect of the arrangement are provided;
- Be incorporated in or governed by the laws of a Member State;
- Be registered with a professional association related to legal, tax or consultancy services in a Member State.

The Directive provides a fairly broad definition of an intermediary, which may apply to almost any person accompanying a transaction. This definition may include lawyers, consultants, accountants, banks, insurance companies, financial consultants, corporate administrators, and other service providers.

It should be noted that DAC 6 is a general directive which Member States are required to implement in their national legislation. It is also expected that Member States will issue guidelines with detailed information about who exactly and how will disclose information as an intermediary, what will be the methodology for recognizing a reportable transaction.

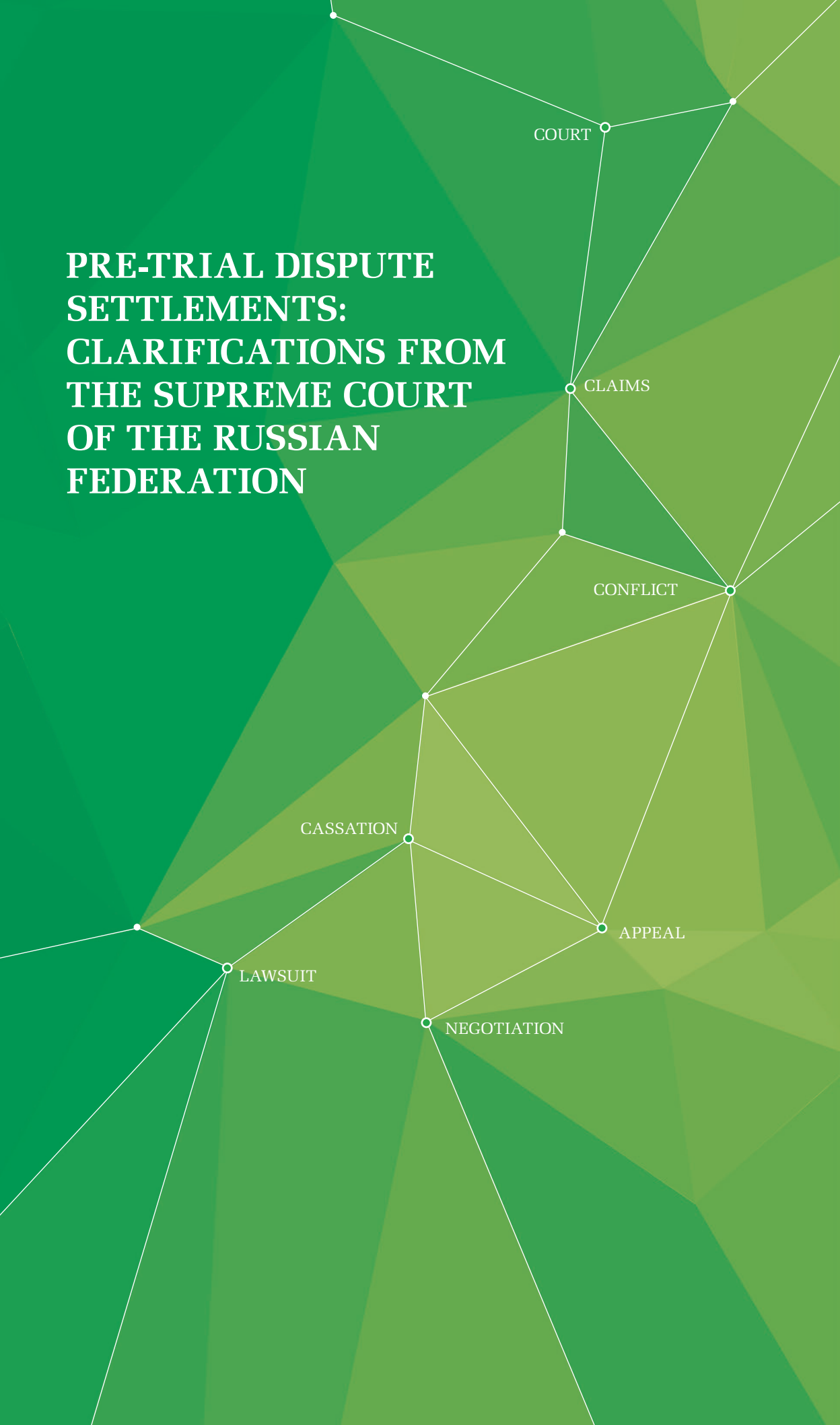
Member States were required to implement DAC 6 in their national legislation by 31.12.2019, and to start applying the new legislation from 01.07.2020; the first reporting on cross-border transactions was to be submitted no later than 30.07.2020, the first reporting on cross-border transactions made between 25.06.2018 and 01.07.2020 was to be submitted no later than 31.08.2020, and the first exchange of information was to take place no later than 31.10.2020. However, 2020 has brought a lot of surprises and the above-mentioned periods were partially shifted to 2021.

To date, the new legislation has been published in most Member States (Austria, Belgium, the Netherlands, France and others), certain states have not yet adopted the legislation which is currently in the draft stage (Cyprus), and certain states have issued guidelines, while a vast majority of Member States has taken advantage of the extension of reporting deadlines.

DAC 6 is a new stage in the evolution of information disclosure, the practi-

cal part of which is not yet developed. In order to determine whether a person is an intermediary or not, to develop a clear understanding of the hallmarks of aggressive tax planning and disclosure methods, to assess risks and consequences of the automatic exchange, it is necessary to review the national legislation and methodological recommendations of a particular Member State.

PRE-TRIAL DISPUTE SETTLEMENTS: CLARIFICATIONS FROM THE SUPREME COURT OF THE RUSSIAN FEDERATION



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At the end of July 2020, the Supreme Court summarized the judicial practice regarding the procedure for pre-trial settlement of commercial disputes. The Supreme Court gave answers to such questions as whether a claim is required before filing a counterclaim, whether negotiations may replace it, whether errors in calculations are allowed in the claim, and many others.

We decided to cover the most important aspects of the said summary in this article.

Pre-trial dispute settlements

Main objectives of arbitration proceedings are not only protection of violated rights and legitimate interests of the parties, but also promotion of initiation and development of business partnerships, as well as the peaceful settlement of disputes and development of business ethics.

One of the ways to achieve these objectives is to apply the pre-trial dispute settlement procedure by the disputing parties, which is aimed at prompt resolution of the conflict.

This procedure is mandatory:

1. If you intend to file a lawsuit to the arbitration court for recovery of money under the agreement or following unjust enrichment;
2. If you need to terminate or amend the agreement through legal action;
3. In cases stipulated by the federal law or agreement, if you claim in the arbitration court:
   - Other property under agreements and other transactions (e. g. goods from a supplier) rather than money;
   - Unjust enrichment in kind (e. g. when you claim the return of a building that you transferred under an uncompleted lease agreement);
   - Money, but not under a transaction or following unjust enrichment (e. g. being a rightholder you claim exclusive rights to compensate for damages or repayment from an offending party).

1. Summary of the practice of application by arbitration courts of the provisions of the procedural legislation on mandatory pre-trial dispute settlement (approved by the Presidium of the Supreme Court of the Russian Federation on 22.07.2020).

In this case, the procedural legislation insists on applying pre-trial settlement measures by the disputing parties. Thus, civil law disputes regarding recovery of funds under claims arising from agreements may be submitted to the arbitration court only after the parties have taken pre-trial settlement measures to settle such a dispute.

The court will not consider a lawsuit if no claim was sent, in case the claimant should have sent it. In this case, the court will:

- Leave a lawsuit without action, and then return it. Initially, the court leaves a lawsuit without action and gives an opportunity to the claimant to provide evidence of compliance with the claim procedure. But since a claim was not sent, the claimant will be unable to fulfill the court's requirement, and a lawsuit will be returned after the expiration of the period set by the court;
- Terminate consideration of the case if it finds that the claim procedure is not followed after accepting a statement of claim for court proceedings. The court may do so on its own initiative or at the request of the defendant.

The court shall return a statement of claim if by the day of the appeal to the court the period of pre-trial dispute settlement established by law or agreement has not expired and there is no response to the claim.

Moreover, if the arbitration court decides that the dispute arose due to a violation of the claim procedure by a person, it will assign legal costs to this person regardless of the judgment on the case.

At the same time, in practice there are cases when implementation of pre-trial settlement measures is unreasonable and unable to achieve the stated goals from the start. The Supreme Court issued clarifications regarding some of these cases.

When is a claim required?

As clarified by the Supreme Court, the claim procedure shall not apply to lawsuits for pledge foreclosure, lawsuits for damages and cases for which the Arbitration Procedure Code of the Russian Federation sets special rules for consideration (corporate disputes, writ proceedings cases, etc.).

Moreover, the Supreme Court mentioned that the assignee's compliance with the pre-trial dispute settlement procedure is not required if this procedure was followed by the original lender before notifying the debtor of the right assignment. Furthermore, when filing a counterclaim it is not required to send a claim if the counterclaim is based on the same legal relationship and the content of the response to the claim shows the substance of the counterclaim.

What is the procedure for filing a claim?

The Supreme Court confirmed that the claim might be sent to the address specified in the agreement (e.g. for correspondence), rather than only to the registered address. If a claim is sent by the Russian Post, it is not required to make a list of enclosures, unless the claimant sent other correspondence to the defendant during this period.

It is possible to send a claim by e-mail if this is expressly provided for in the agreement and the parties have agreed upon the e-mail address to which such a claim may be sent.

In order to avoid missing legally significant messages during personnel changes, it is possible to provide for a common corporate email address for claims correspondence, which may be accessed not only by an employee responsible for working with the counterparty.

What is the procedure for pre-trial dispute settlement?

The procedure for pre-trial dispute settlement should be specified in detail in the agreement.

Numerous agreements include a general provision for dispute settlement through negotiations, but in the absence of details it does not exclude the necessity to file a claim.

The procedure for negotiations or mediation should be regulated in detail by the agreement in order for the relevant actions to be qualified as compliance with the non-pre-trial dispute settlement procedure.

The claim procedure is deemed to be complied with in case of an arithmetic error in the claim or an increase in the period for calculating the penalty after the claim is filed.

The discrepancy between the amounts in the claim and the lawsuit does not constitute a violation if the claim specifies the circumstances on which the claim is based and the relevant terms of the agreement, and the difference in the claimed requests is due to an error in calculations or a continuing delay in performance.

When drawing up claims it is required to describe in detail grounds for claims with reference to the primary documents and the relevant terms of the agreement. Periods of occurrence of the principal debt and the amount of debt for each of the periods that expired at the time of sending the claim should be definitely specified in the claim.

What are the terms?

Pre-trial settlement suspends the statute of limitations.

The party's compliance with the requirements for mandatory pre-trial dispute settlement suspends the statute of limitations for the period of actual compliance with the claim procedure. A failure to receive a response to the claim within 30 days, or any other period set by the agreement shall be qualified as a refusal to satisfy the claim received on the 30th day or on the last day of the period set by the agreement.

A failure to comply with the deadline for pre-trial settlement may result in a refund of the claim, filing a claim to the court before the deadline for consideration of the claim has expired, provided that the response to it has not been received, hinders the consideration of the dispute.

The Supreme Court emphasizes that the pre-trial settlement period should expire by the time the documents are filed to court. One should not expect the pre-trial settlement period to expire by the time the issue of accepting a lawsuit for court proceedings is resolved. It is required to declare non-compliance with the pre-trial procedure in the court of first instance.

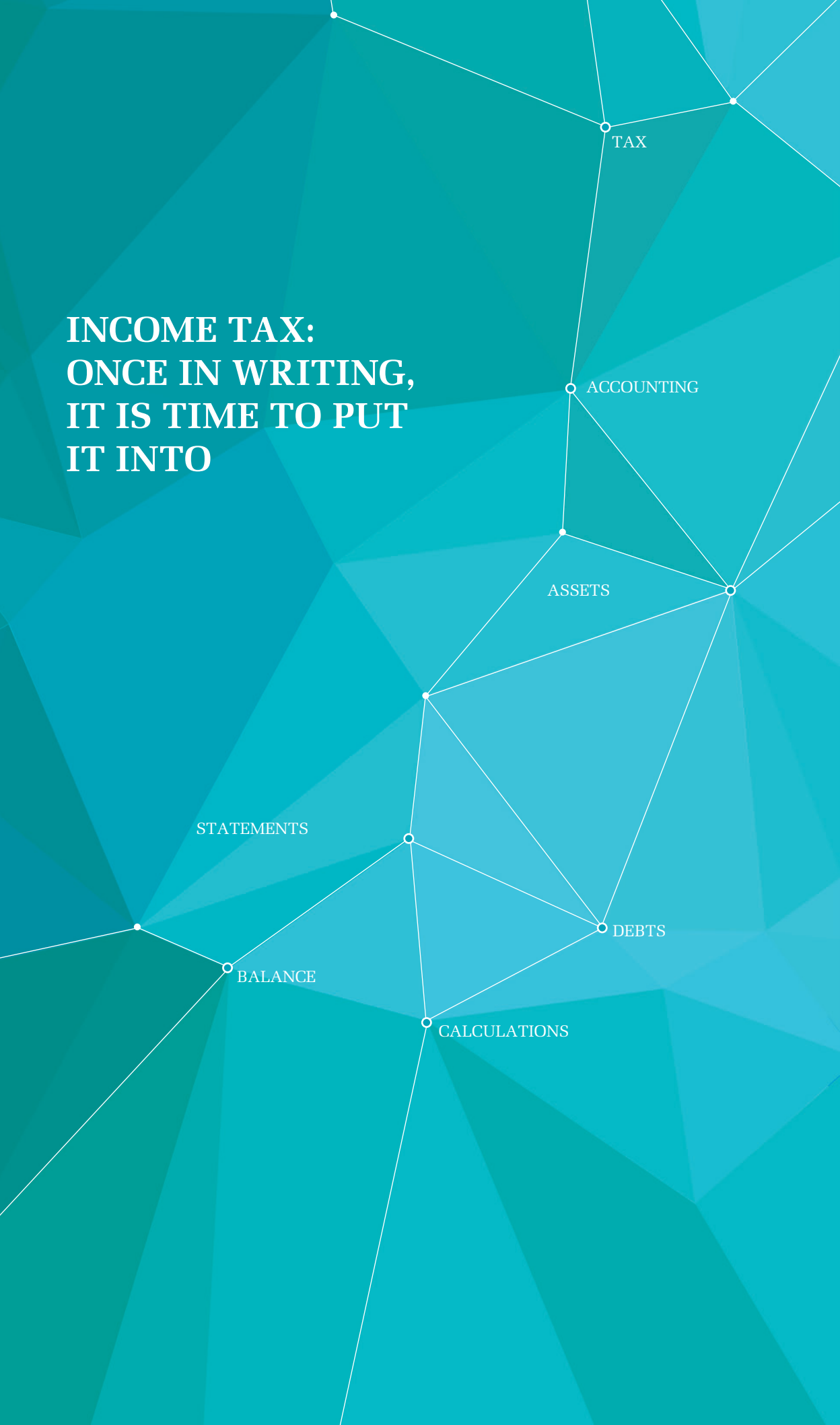
The argument about non-compliance with the pre-trial dispute settlement procedure should be submitted by the defendant only in the court of first instance. Otherwise, the defendant loses the right to refer to the relevant circumstances in the courts of appeal and cassation.

The result of this summary is obvious: rules of the procedural legislation on pre-trial dispute settlement should not be interpreted from a purely formal point of view. The court needs them to make sure that pre-trial attempts to resolve the legal conflict have been exhausted subject to the assessment of the circumstances.

This approach seems to be consistent with the goals of legal regulation and creates no unreasonable obstacles to the exercise of rights by bona fide participants of civil law transactions.

At the same time, it seems imperative to abandon the practice of including meaningless phrases, such as "all disputes shall be resolved through negotiations" into agreements. Instead, it is advisable to spend some time and effort on truly coherent and consistent pre-trial settlement procedures and inclusion of a "working" condition into the agreement. A

INCOME TAX: ONCE IN WRITING, IT IS TIME TO PUT IT INTO



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In November 2018, the Ministry of Finance of the Russian Federation amended Accounting Regulations "Accounting for Corporate Income Tax" PBU 18/02 (hereinafter, PBU 18/02), which are mandatory for accounting statements for 2020, i. e. for accounting from January 1, 2020.

It became possible to apply the revised version on a voluntary basis from January 1, 2019.

We shall begin by covering the most significant changes made to PBU 18/02. We shall omit formalities and rules introduced for consolidated groups of taxpayers.

New terms — old substance

It should be noted that two terms were replaced throughout PBU 18/02:

Previous version	Revised version
Permanent tax liability	Permanent tax expenses
Permanent tax asset	Permanent tax income

Permanent became temporary

Below is the comparison between reasons for temporary differences in the previous and revised versions (table 1).

Table 1

Previous version. Temporary differences arise from:	Revised version. Temporary differences arise from:
Applying different methods of depreciation accrual for accounting purposes and for purposes of determining income tax	Applying different rules for estimating the initial cost and depreciation of non-current assets for accounting and tax purposes

Table 1

Previous version. Temporary differences arise from:	Revised version. Temporary differences arise from:
Applying different methods of recognition of Commercial and administrative expenses in the cost price of sold products, goods, works, and services in the reporting period for accounting and tax purposes	Applying different methods of generating the Cost price of sold products, goods, works, and services for accounting and tax purposes
Loss carried forward that was not used to reduce income tax in the reporting period, but which will be accepted for taxation in subsequent reporting periods, unless otherwise provided for by the legislation of the Russian Federation on taxes and levies	Loss carried forward that was not used to reduce income tax in the reporting period, but that will be accepted for tax purposes in subsequent reporting periods
Applying, in case of the sale of fixed assets, different recognition rules for accounting and tax purposes of the residual value of fixed assets and expenses related to their sale	Applying, in case of the sale of fixed assets, different recognition rules for accounting and tax purposes of income and expenses related to their sale
Payables for purchased goods (works, services) using the cash method of determining income and expenses for tax purposes, and for accounting purposes — based on the assumption of temporary certainty of business facts	None
Recognition of revenue from the sale of products (goods, works, services) as income from ordinary activities of the reporting period, as well as recognition of interest income for accounting purposes based on the assumption of temporary certainty of business facts, and for tax purposes — using the cash method	None
Applying various rules for recording interest paid by an organization for funds (credit facilities, loans) granted thereto for accounting and tax purposes	Applying various rules for recording interest paid by an organization for funds (credit facilities, loans) granted thereto for accounting and tax purposes
None	Revaluation of assets at the market value for accounting purposes
None	Recognition of impairment of financial investments for which the current market value is not determined, inventory and other assets in accounting records
None	Applying different rules for creating a provision for doubtful debts and other similar provisions for accounting and tax purposes
None	Recognition of estimated liabilities in accounting records
Other similar differences	Other similar differences

The table above shows that the revised version of PBU 18/02 expressly refers to the following business facts as temporary differences:

- Revaluation of assets for accounting purposes;
- Impairment of financial investments for accounting purposes;
- Differences between the rules for creating a provision for doubtful debts;
- Recognition of estimated liabilities.

Before the changes came into force, due to the lack of clear legal instructions an accountant had a choice regarding the classification of the said facts as temporary and permanent.

For example, in practice, differences in creating a provision for doubtful debts, provision for vacation payments, and provision for impairment of inventory for accounting purposes only were classified as permanent differences to simplify accounting. Now an accountant has no such option.

Permanent differences are now created only if income and/or expenses recognized for accounting purposes are never recognized for tax purposes and vice versa.

In other words, in accounting creating temporary differences is a feature, while creating permanent differences is an exception.

New calculation of differences

Prior to 2020, the practice of corporate income tax accounting meant determining permanent and temporary differences for income and expenses. The revised version introduces the balance method, which implies determination of temporary differences based on the difference between the book value of an asset (liability) and its value accepted for tax purposes.

This method provides for an option to refuse from the detailed recognition of permanent and temporary differences for each operation, although it does not prohibit their recognition in accounting.

Accounting options and accounting policy

A method of determining current income tax is fixed in the accounting policy of an organization. An organization may use the following methods to determine current income tax:

- Based on accounting data;
- Based on the income tax return.

In both cases, the amount of current income tax should correspond to the amount of the calculated income tax reflected in the corporate income tax return.

The method of determining current income tax based on accounting data (cost method) is a customary method used before the changes became effective.

The method of determining current income tax based on the income tax return (balance method) became widespread only after the changes considered herein became effective.

Therefore, given that the method of determining current corporate income tax based on accounting data remained in PBU 18/02, an organization may keep the customary method of determining current income tax, if it secures such a method in its accounting policy. However, this method is only applicable if the result corresponds to the calculation under the balance method. The cost method is based on the analysis of income and expenses, which makes it inconvenient as during each reporting period an accountant will have to conduct an audit calculating differences using the balance method. Accountants will have to develop their own methodology and will most likely need to maintain additional tables to account for arising differences.

Therefore, despite the frightening uncertainty of the new balance method, it is still worth changing the accounting method for corporate income tax from cost to balance one.

Retrospective restatement of balances

In accordance with the provisions of PBU 1/2008 "Accounting Policies of Organizations" changes in the accounting policy that significantly affect indicators of accounting statements should be reflected in the accounting statements retrospectively.

Retrospective recognition of consequences of changes in the accounting policy is adjusting the incoming balance under the item "Retained Earnings (Retained Loss)" and/or other balance sheet items as of the earliest date presented in the accounting (financial) statements, as well as values of related accounting items disclosed for each period presented in the accounting statements, as if the new accounting policy was applied from the moment of occurrence of the business facts of this type.

In other words, if the method of determining current corporate income tax is changed, an accountant will have to calculate the impact of changes on accounting statements and if such changes are significant will have to restate comparable data in the accounting statements for 2020.

Software and features of transaction

1C Program (section "Accounting Policy") currently provides for three accounting methods for corporate income tax:

- Balance method;
- Balance method with recognition of permanent and temporary differences;
- Cost method.

As mentioned above, it is not advisable to use the cost method. Moreover, it is prohibited for use by organizations with separate divisions that apply different corporate income tax rates.

The balance method has two options: with and without recognition of permanent and temporary differences. The difference between them is that when using the balance method no "familiar" permanent differences and temporary differences will be formed.

If an accountant wants to keep them, then he/she will have to opt for the balance method with recognition of permanent and temporary differences.

When switching from the cost method to the balance method, provided that accounting and tax records are correctly formed, the program should automatically recalculate balances of accounts 09 "Deferred Tax Asset" and 77 "Deferred Tax Liability" in correspondence with account 84 "Retained Earnings (Retained Loss)" at the beginning of the period.

Practice of the balance method

Based solely on the text of PBU 18/02, it is not clear how to apply the new rules in practice. There are no official interpretations for the revised version of PBU 18/02, so it is possible to apply Recommendation P-102/2019-КпР "Procedure for Income Tax Accounting", which was issued in April 2019 by Foundation "National Non-Governmental Accounting Regulator "Accounting Methodological Center" (hereinafter, the Recommendation). The said Recommendation was approved by the Committee on Recommendations. The text is published on the official website of the Foundation.

Thus, in accordance with this Recommendation the amount of income tax expense is formed on the debit of account 99 "Profit and Loss" (in case of tax income — on the credit). The specified amount includes two components: current income tax and deferred income tax. It is recommended to account for each of the components on a separate subaccount to account 99.

The amount of current income tax is recognized on the debit of account 99 "Profit and Loss" (sub-account "Current Income Tax") in correspondence with the credit of account 68 "Calculations of Taxes and Fees" (sub-account "Calculations of Corporate Income Tax"). The specified amount is determined in accordance with requirements of the tax legislation as the amount of tax payable to the budget for the tax period corresponding to the reporting period. Such amount (in the absence of specific circumstances) corre-

sponds to the amount of tax specified by an organization in its income tax return for the corresponding period.

The amount of deferred income tax is recognized on the debit or credit of account 99 "Profit and Loss" (sub-account "Deferred Income Tax") in correspondence with the credit or debit of accounts 09 "Deferred Tax Assets" or 77 "Deferred Tax Liabilities" respectively.

If temporary differences change due to retrospective changes in the accounting policy or retrospective corrections of errors, the resulting changes in deferred tax assets or liabilities are recognized on the debit or credit of accounts 09 "Deferred Tax Assets" or 77 "Deferred Tax Liabilities" in correspondence with the credit or debit of account 84 "Retained Earnings (Retained Loss)" respectively.

Therefore, after the revised version of PBU 18/02 becomes effective, all corporate income tax transactions shall be collected on account 99 "Profit and Loss" for accounting purposes. Previously, deferred tax assets and liabilities were recognized in correspondence with account 68 "Calculations of Taxes and Fees", and in order to prepare the statement of financial results amounts had to be collected from several accounts (at least for verification). Now the entire calculation of income tax is recognized on one account.

Below is the comparison of accounting records according to previous and revised rules (table 2):

The table above shows that now recognition of corporate income tax in accounting is based not on accounting data, but on data in corporate income tax returns. If previously the main account for corporate income tax accounting was account 68 "Calculations of Taxes and Fees", now it is account 99 "Profit and Loss". Account 68.04.2 "Calculation of Income Tax" is not used in the balance method (without recognition of permanent and temporary differences).

Table 2

Transaction description	Previous version		Revised version		Note
	Debit	Credit	Debit	Credit	
Provisional income tax expenses	99	68	99	68	**Previously:** current income tax consisted of two parts recognized on account 68: provisional expense (income) and PTL/PTA. **Now:** a record is made for calculating the current corporate income tax corresponding to the corporate income tax return.
Provisional income tax income	68	99	68	99	
Recognition of DTA	09	68	09	99	**Previously:** deferred tax assets and liabilities were recognized in correspondence with account 68. **Now:** deferred tax assets and liabilities are collected on account 99.
Derecognition of DTA	68	09	99	09	
Recognition of DTL	68	77	99	77	
Derecognition of DTL	77	68	77	99	
Permanent tax liability (PTL)	99	68	—	—	**Previously:** PTL/PTA were recorded on account 99 on a separate sub-account. **Now:** PTL/PTA is not recognized in accounting.
Permanent tax asset (PTA)	68	99	—	—	

Summary

Therefore, starting from 2020 organizations, with the exception of those not covered by PBU 18/02 or those applying simplified accounting and reporting methods, are required to apply the new accounting rules for corporate income tax calculations.

Temporary differences now prevail in accounting, while permanent differences occur in exceptional cases.

With the new balance method accounting should become clearer, more transparent, and less tedious. However, when applying this method an accountant will have to calculate the effect on the indicators of accounting statements and, if necessary, retrospectively recalculate comparable data in the accounting statements for 2020.

Despite the obligation to apply the amendments, the revised version of PBU 18/02 does not prohibit the use of the customary cost method. The only note is that the use of the cost method is possible if the calculation of income tax using the cost method does not differ or insignificantly differs from the amount of income tax calculated using the balance method.

Correct tax accounting is a prerequisite for automatic calculation of temporary differences. Otherwise, an accountant will have to manually keep registers for calculating temporary differences. A

About the Company

Korpus Prava was established in 2003 in Moscow, Russia. Together with our offices in Russia, Cyprus, Latvia and Hong Kong we offer clients a truly international service. Our highly qualified and friendly staff is available to provide to the clients a flexible, reliable and efficient service.

The mission of the Company is to raise the business value of the client and bring down risks.

Korpus Prava offers services in:

- Legal and tax consulting
- Transformation of financial statements to IFRS
- International tax planning
- Project consulting
- Corporate services
- Capital transactions / M&A
- Tax disputes
- Economic disputes and bankruptcy
- Real estate transactions
- Intellectual property
- Financial Consulting

The company is mentioned in the rankings of the leading international directory "Legal 500" that is completely and comprehensively overtaking the global scope of legal services.

Korpus Prava was nominated as the best legal firm in Russia according to the authoritative magazine "The Lawyer"; it takes one of the leading positions amongst Top 50 legal firms in Cyprus, and it has also been recognised as the best international legal firm for tax planning in Cyprus. Korpus Prava Private Wealth Practice has taken fifth place in Private Banking and Private Wealth sector in Russia, in the category of Succession Planning Advice and Trusts according to the annual rankings of Private Banking Russia Survey 2016 of the prestigious magazine "Euromoney" (as of February, 2016).

Korpus Prava is a member of Cyprus Fiduciary Association (CFA) and Franco-Russian Chamber of Commerce and Industry (CCIFR). It takes part in the development of business community, business presentations and the exchange of professional experience.

Our certified specialists conduct seminars and consultations for accountants and the representatives of company financial services; they act as experts, and they are published in popular financial publications.

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