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Global Tax Alert

News from Transfer Pricing

Russia issues draft Procedure on multilateral APAs

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Executive summary

On 3 March 2017, the Russian Finance Ministry published a draft Procedure outlining the process for handling multilateral Advanced Pricing Agreements (APAs).

The Procedure is intended to enable a taxpayer to conclude an APA in relation to a foreign trade transaction with Russia's tax treaty partner countries. The adoption of the Procedure should provide a practical framework for the conclusion of a bilateral and/or a multilateral APA with the involvement of a foreign competent authority. Such APAs may prevent transfer pricing disputes, as recommended, inter alia, by Action 14 of the Organisation for Economic Co-operation and Development's (OECD) Base Erosion and Profit Shifting Action Plan.

Development of the Procedure is required by the Russian Tax Code in order to enable the conclusion of bilateral or multilateral APAs. Although such APAs are technically allowed for any large taxpayer since 2012, to date the Russian tax authorities have signed only unilateral APAs and they are predominately related to domestic transactions.

Public discussion of the Procedure will end on 17 March 2017. The Procedure is to be enacted within one month after it is officially published.

Detailed discussion

The Russian Finance Ministry is regarded as the competent tax authority of Russia for purposes of tax treaties. As far as bilateral or multilateral APAs are concerned, the Ministry is going to delegate the competent authority powers to the Federal Tax Service (FTS) which will enable the FTS to conduct mutual agreement procedures with competent tax authorities of tax treaty partner countries.

The Procedure sets out the following stages of the bilateral APA process.

Preliminary discussion with the FTS

This stage is generally informal and optional. The results of the preliminary discussion are not binding on the taxpayer or on the FTS. Whatever the outcome of the preliminary discussion, the taxpayer may still apply to the FTS for the conclusion of an APA in relation to foreign trade transactions.

Formal application

The Procedure contains the recommended form of an APA application and a list of documents required to initiate the APA process. The list of documents is open but should include, among others, a draft of the APA wording, whereby the Ministry has suggested a possible APA structure as a guidance. It follows therefore that the taxpayer must, *inter alia*:

- ▶ Demonstrate the application of the suggested transfer pricing methodology by reference to the last three years and by reference to periods to be covered by the APA (based on available forecast data)
- ▶ Specify critical assumptions for the purposes of an APA

Under the Procedure, a formal APA application should be submitted in both jurisdictions in order for the FTS to commence communication with the competent authority of the other state. All documents (information) submitted to the foreign competent authority must also be presented to the FTS.

FTS consideration of the taxpayer's application

At this stage the FTS may conduct:

- ▶ Discussions with the taxpayer on matters relating to the conclusion of the APA
- ▶ Mutual consultations with the foreign competent authority

The FTS will consider the application from the standpoint of whether:

- ▶ The proposed transfer pricing methodology meets the arm's length standard as outlined by the Russian Tax Code
- ▶ The proposed pricing methodology enables the elimination of double taxation
- ▶ In the absence of an APA, there are uncertainties or significant technical issues related to the pricing approach
- ▶ A transaction is of a long term nature
- ▶ There is the possibility of an unjustified tax benefit as a result of the transaction

Negotiations between competent authorities

An important stage in the process of the conclusion of a pricing agreement is the conduct of negotiations between the FTS and the foreign competent authority, which may result in a mutual agreement between them.

A copy of the mutual agreement itself is not made available to the taxpayer, but is used as a basis for signing an APA with the taxpayer at a later stage in the process. If a mutual agreement cannot be reached with the foreign competent authority, it is still possible for the FTS and the taxpayer to conclude a unilateral APA, without the involvement of the foreign competent authority.

Implementation of the mutual agreement of the competent authorities

If a mutual agreement is reached between the FTS and the foreign competent authority, the FTS will suggest to the taxpayer the conclusion of an APA on the terms agreed to in the mutual agreement or to amend the draft APA in order to comply with the mutual agreement. If the taxpayer agrees, an APA will be concluded.

Implications

For the Procedure to be effective in practice, there are a number of important issues to still be addressed.

One example is the arm's length standard which is to be followed by the FTS in its negotiations with the foreign competent authority and whether the standard will be set by reference to the Russian Tax Code (as currently stands in the Procedure) or the OECD Transfer Pricing Guidelines (which may be a preferred scenario enabling some consensus).

The timing of the bilateral/multilateral APA process may also be very relevant to the practical implication of the Procedure since, based on worldwide APA practices, the current timing set for APAs in the Russian Tax Code (up to nine months for internal review by the tax authority) is unlikely to be sufficient for the bilateral or multilateral process. It is possible that resolving some of these issues may require amendments to the Russian Tax Code.

For additional information with respect to this Alert, please contact the following:

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